THE CHANGING ROLES OF THE STATE AND TRANSNATIONAL CORPORATIONS IN THE DEVELOPMENT OF MINING IN ZAMBIA: AN EVALUATION OF INFLUENCES ON THE TRANSITION FROM STATE TO PRIVATE OWNERSHIP OF THE MINING SECTOR

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DECLARATION

I, Rahima Ahmed, declare that this research report is my own unaided work. It is submitted in partial fulfillment of the requirements for the degree of Masters in Economics (100%) at the University of the Witwatersrand, Johannesburg. It has not been submitted before for any degree or examination in this or any other university.

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Rahima Ahmed, July 2010.

Dedication

I dedicate this work to my parents and friends that supported me through the process.

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AAC	Anglo American Corporation
AVMIN	Anglovaal Mining Limited
BFB	Basic Food Basket
BNB	Basic Needs Basket
BoZ	Bank of Zambia
BSA	British South African Company
Capex	Capital Expenditure
CDC	Commonwealth Development Corporation
CDF	Copperbelt Development Foundation
CEC	Copperbelt Energy Corporation
CGIC	Credit Guarantee Corporation (of South Africa)
CIPEC	*Council Intergovernmental des Pays Exportateurs Cuivre* (Intergovernmental Council for Copper Exporting Countries)
COMESA	Common Market for Eastern & Southern Africa
CRC	Constitution Review Commission
CRO	Chingola Refractory Ore
DBZ	Development Bank of Zambia
DCDM	De Chazal Du Mée
DFI	Direct Foreign Investment
DHMBs	District Health Management Boards
DLA	Defense Logistic Agency
DRC	Democratic Republic of Congo
EPB	Economic Planning Board
ECZ	Environmental Council Zambia
ESAF	Extended Structural Adjustment Facility
FDI	Foreign Direct Investment
FEMAC	Foreign Exchange Mechanism Allocation System
FNDP	Fifth National Development Plan
FSDP	Financial Sector Development Plan
FTA	Free Trade Area
GRZ	Government of the Republic of Zambia
GRZ/ZCCM-PNT	Government of the Republic of Zambia/Zambia Consolidated Copper Mines-Privatisation Negotiation Team
HDI	Human Development Index
HFO	Heavy Fuel Oil
HIPC	Highly Indebted Poor Country Initiative
HPI	Human Poverty Index
IDA	International Development Association
IDC	Industrial Development Corporation (of South Africa)
INDECO	Industrial Development Corporation (of Zambia)
IFC	International Finance Corporation
IFls	International Financial Institutions
ILO	International Labour Organisation
IMF	International Monetary Fund
INDP	Interim National Development Plan
ISO	International Organisation for Standardisation
ISI	Import Substitution Industrialisation
JCTR	Jesuit Centre for Theological Reflection
KCM	Konkola Copper Mines
KDMP	Konkola Deep Mining Project
LCM	Luanshya Copper Mines
LME	London Metal Exchange
LuSE	Lusaka Stock Exchange
MBOs	Management Buy Outs

MCM	Mopani Copper Mines
MDRI	Multilateral Debt Relief Initiative
MINDECO	Mining Development Corporation
METR	Marginal Effective Tax Rate
MFEZ	Multi-Facility Economic Zone
MIMACO	Mineral Marketing Corporation
MMD	Movement for Multiparty Democracy
MRG	Metal Resource Group
MRDI	Mineral Resources Development International
MUZ	Mineworkers' Union of Zambia
NCCM	Nchanga Consolidated Copper Mines
NCDP	National Commission for Development Planning
NERP	New Economic Reform Programme
NFC	Non-Ferrous Metal Industry
NFCA	Non-Ferrous Company-Africa
NGO	Non-Governmental Organisation
NLC	Ndola Lime Company
NTB	Non-Tariff Barriers
NUMAW	National Union of Miners and Allied Workers
OECD	Organisation of Economic Cooperation and Development
PAYE	Pay As You Earn
PIRC	Privatisation and Industrial Reform Credit
PFP	Policy Framework Paper
PRA	Privatisation Revenue Account
PRGF	Poverty Reduction and Growth Facility
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
PTA	Preferential Trading Area
RAP	Rights Accumulation Program
RAMCOZ	Roan Antelope Mining Corporation of Zambia plc
RCM	Roan Consolidated Copper Mines
RST	Roan Selection Trust
SADC	Southern African Development Community
SAPs	Structural Adjustment Programmes
SDR	Special Drawing Rights
SOEs	State-Owned Enterprises
TB	Treasury Bills
TNDP	Transitional Development Plans
TNCs	Transnational Corporations
TST	Technical Support Team
TAZARA	Tanzania Zambia Railway
TVEs	Township and Village Enterprises
T/y	Tons per year
UDI	Unilateral Declaration of Independence
UNDP	United Nations Development Programme
UNIP	United National Independence Party
VAT	Value-Added Tax
WTO	World Trade Organisation
ZACCI	Zambia Association of Chambers of Commerce and Industry
ZAM	Zambia Association of Manufacturers
ZCCM	Zambia Consolidated Copper Mines
ZCCM-IH	Zambia Consolidated Copper Mines-Investments Holdings plc
ZCI	Zambia Copper Investments (a subsidiary of Anglo American)
ZCTU	Zambia Congress of Trade Unions
ZDA	Zambia Development Agency
ZESCO	Zambia Electricity Supply Corporation

ZIC	Zambian Investment Centre
ZIMCO	Zambia Industrial and Mining Corporation
ZANACO	Zambia National Commercial Bank
ZNOC	Zambia National Oil Company
ZAMEFA	Metal Fabricators of Zambia Limited
ZPA	Zambia Privatisation Agency
ZRA	Zambia Revenue Authority

Abstract

This dissertation principally analyses: (i) the privatisation of Zambia's copper mines; (ii) the impact of state and private ownership and control of the mines on development; and (iii) the roles of mining TNCs in the Zambian economy. The research covers the period from independence in 1964 to 2006/7, but mainly focuses on the 1991 to 2006/7 period. The validity of several neo-classical theoretical views and counter-arguments pertaining to the social and economic benefits of privatisation and the private ownership and the activities of mining TNCs is tested in the mining sector study. The methodology is based on a case study comprising fieldwork and literature research, utilising a qualitative approach and an inductive method. The conclusions of the study could enhance knowledge from which other developing countries intent on privatising their SOEs could draw, as privatisation studies of sub-Saharan countries have mostly overlooked analyses of the social impact of the private ownership of enterprises. Key findings of the study are that the privatisation and private ownership of the mines by TNCs have failed to produce net positive socio-economic outcomes for Zambia. Furthermore, under private ownership of the mines, the political-economic benefits have shifted, mainly concentrating the surpluses from mining in favour of mining TNCs. The primary recommendations from the study are that certain measures, in particular a strong state capacity, are fundamental in enabling greater and more equitable redistribution of benefits for the country from privatisation, private ownership and the economic activities of mining TNCs.

Keywords: Zambia, mining, privatisation, private ownership, state ownership, TNCs, state capacity.

CHAPTER 1

1. INTRODUCTION

The dissertation investigates the changing roles of the state and transnational corporations (TNCs) in the development of mining in Zambia. The investigation includes an evaluation of influences in the transition from state to private ownership of the mining sector. The shifts in economic and political power (viz. the political economy) and the social impact linked to these policy changes further represent important components of the study. The copper mining sector of Zambia is used as a case study to examine these economic issues.

Copper mining has been the backbone of the Zambian economy as the major earner of Zambia's exports and historically as a significant generator of economic activity and of development. Furthermore, the mining sector and its backward linkages in the Copperbelt have employed a large number of the workforce. This has further contributed to the Copperbelt acquiring substantial political significance. The ownership of the mines shifted from private to state ownership and reverted to private ownership in 2000. Anglo American possessed full ownership of a sizable part of the mines under private ownership. Moreover, prior to the privatisation of the mines under majority state ownership, Anglo American still retained just over a quarter of the shareholding in the mines.

The large-scale privatisation of the mines in Zambia and the consecutive changes in ownership and management control that the mining sector has undergone between the state and TNCs, make the Zambian mining sector a pertinent case study for investigating issues such as privatisation and state and private-sector control of enterprises. The mining TNCs' majority ownership of the Zambian copper mines also renders this sector suitable for a study of the roles of TNCs. The research paper has adopted a case study approach to the Zambian copper mines and mainly tests observed events in the sector against various theoretical arguments pertaining to the issues under investigation. An overview of the study, the context of the Zambian mining sector and the chapter outline are set out below.

1.1 OVERVIEW OF THE STUDY

This section delineates the research aims and questions, definitions, the rationale, scope, main theoretical arguments and the contributions of the study.

1.1.1 Research aims and research questions

The core research aims of the study are to investigate (i) the privatisation process of the copper mines; (ii) the influence of changes in ownership and management control on the development of Zambia; (iii) the roles of significant actors, in particular the state and the mining TNCs, in the mining sector; and (iv) the socio-economic and political-economic impact of the roles of TNCs and of the government on the copper mines and the Zambian economy.

The main secondary research questions the study aims to answer are as follows:

- What were the various policy approaches of the different governments for the mining sector in particular under state and private ownership of the mines and in the privatisation of the mining sector and what were their development consequences?
- What were the outcomes of changing ownership and management control for the growth and socio-economic development of the mining sector?
- What roles did the mining TNCs play in the copper mining sector within a weak state and how did their activities affect the development of the mining sector and the Zambian economy?
- What was the capacity of the Zambian state in ensuring positive outcomes for Zambia from the privatisation of the copper mines and from the activities of mining TNCs?
- How did different government policies and the activities of mining TNCs influence the political economy of Zambia?

1.1.2 Definitions and clarification of terms

Since the mining of copper and cobalt, a by-product of copper, accounts for over 90% of the total mining contribution to the Zambian economy, making it highly representative of the mining industry in Zambia, references to the mining sector in the study pertain largely to copper mining. Furthermore, the term ‘development’ for the mining sector as employed in the paper, implies a combination of higher output levels, increases in employment, higher government revenue from mining (net of subsidies and concessions), and the viable operation of mining without subsidies. Broadly, the author has used the term ‘privatisation’ to refer to the processes involved in transferring ownership of the state-owned enterprises (SOEs) from the public to the private sector; it therefore precedes private ownership. Private ownership refers to the enterprise under the ownership of the private sector.

1.1.3 Rationale for the study

The widespread privatisation of the majority state-owned copper mining sector in Zambia makes the sector a useful case study for examining the privatisation process and its consequences in the context of a weak state. Moreover, comparisons afforded through the changes in ownership and management controls of the Zambian copper mining sector from 1963, the year before independence, to 2008, also make the Zambian mining sector a suitable case study for gaining broad insight in the roles of different combinations of ownership and management controls. The study further provides clarity on the impact of the changes in ownership and management structure on the development and the political economy of Zambia.

The ownership of the mines in Zambia shifted from private ownership during colonial rule, extended into the ‘Accommodation Period’ until 1969, and to majority government ownership of the mines, from 1969 to 1996. Zambia experimented from 1969 to 1973 with private management and majority government ownership of the mines. Subsequently, both majority ownership and the management of the mines were transferred to the government until the mines were privatised under Chiluba’s government. The privatisation of the mines took place from 1997 until 2000. TNCs took over majority ownership and management control of the mines since the mines were privatised.

Furthermore, the majority ownership of the copper mines by TNCs, under private ownership before the mines were nationalised in 1969 and again from March 2000,[1] makes the copper mining sector a pertinent case study for examining the roles of large mining TNCs as powerful actors in the economies of developing countries. Moreover, the study enables the identification of various shortcomings in the capacities and policies of the government in the privatisation process and in its dealings with mining TNCs. The identification of these provides an insight into the preconditions for ensuring more favourable gains for a country from the privatisation of SOEs and from the participation of TNCs in host countries. Additionally, an understanding of the political-economic outcomes linked to the changes in ownership and the activities of TNCs in the mining sector informs on the shifts in economic power linked to the changes in ownership, manager control and to the reallocation of the returns from surpluses of copper sales with the participation of mining TNCs in Zambia.

1.1.4 Scope of the study

The focus of the dissertation is primarily on the period from 1991, when the Chiluba government came into power, until 2006/7. The investigation is nevertheless evaluated in the context of state policies and other significant factors that affected the mining sector during Kaunda's rule (1964-91). Some of these policies and factors also influenced events after 1991. The case study approach enables the unravelling of the influences of significant actors and elements other than ownership that affected the performance of the mining sector. A greater understanding of these influences enables a more accurate and holistic account of the complex interplay of the various issues that affect the performance and development of the mining sector.

Methodological and statistical challenges render the effects of private ownership on performance difficult to determine within the confines of the study. Challenges include the difficulties of comparing the performance of enterprises pre- and post-privatisation or to obtain a counterfactual scenario (what would have happened in the absence of privatisation). Moreover, the selection of appropriate variables to assess performance is

[1] The first mines were privatised in 1997. It is also important to note that Anglo American possessed minority shares in the mines under state majority ownership.

not obvious. Other factors apart from ownership, in particular the price of copper, are also likely to affect enterprise performance, making it difficult to isolate the influence of ownership on performance (Buchs, 2003:16). The reluctance of several private mining companies to divulge information on their profits and losses has also precluded profit-based analyses of performance within the confines of the study. Performance measures may furthermore suffer from a demonstration effect, in which case short-term trends in performance improvements may be misleading, as these may not necessarily play out in the longer term (Villalonga, 2000, cited in Kirkpatrick & Parker, 2005:56).

A lack of adequate statistics has prevented a quantitative cost-benefit analysis of performance. Moreover, at times, gaps in statistics obstruct the construction of trends on a continuous time-series basis, also making comparisons difficult. However, the study uses statistics mainly to describe events, rather than to analyse causality.

1.1.5 Theoretical arguments employed in the study

The dissertation mostly tests the validity of various theories, literature reviews and empirical studies against events in the mining sector case study, enabling the identification of theories that provide the best explanation of observed trends. The research question on the privatisation of the mining sector is mainly assessed against certain institutional and legal prerequisites and government policies considered by several theorists as crucial for ensuring more beneficial outcomes from privatisation. Kenneth Arrow's groundbreaking work concludes that privatisation is secondary in importance to competition (which is, however, not relevant in the resource sector)[2] and the creation of institutional infrastructure for a market economy (Stiglitz, 1998:19, 20; 2002:182). The prerequisites noted by Stiglitz (1998, 2002) and extracted from empirical studies identifying the strengths and weaknesses of privatisation policies, especially of sub-Saharan Africa (Buchs, 2003), Eastern European countries and of China, are mostly employed to assess the privatisation of the mines in Zambia.

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2 As the price is determined on the LME.

The development outcomes of privatisation policies of the mines in Zambia are primarily examined against the neo-classical argument (also of the World Bank) that privatisation and private ownership of SOEs improve public finances, and counter-arguments that gains in public finances are not inevitable. Rather than merely owing to privatisation and private ownership, improvements in public finance are also significantly influenced by the sale price of the SOEs (Cook & Kirkpatrick, 2000a; Pennings, 2008) and sufficient tax payments from the newly privatised enterprise (Buchs, 2003). Moreover, privatisation has been less decisive than profound tax administration reform for revenue performance. Tax evasion tactics of private firms and weaker tax administration of the government under private ownership would lower tax revenue (Buchs, 2003). Tax concessions would also reduce tax revenue under private ownership (World Bank, cited in Cook & Kirkpatrick, 2000b). Benefits in public finance are further more likely if investments are made compulsory and if the government retains shareholdings (Pennings, 2008).

The main theories and empirical studies deployed in addressing the second research question pertaining to the influences of changing management structure and ownership on the growth and socio-economic development of the mining sector are:

(i) The neo-classical argument that changing objectives under different ownerships, namely the electoral-maximising motives of the government in SOEs and the profit-maximising motives of the shareholders in private companies, promote greater *x*-efficiency in private companies over SOEs. Greater *x*-efficiency contributes to the better performance of private-owned enterprises (Lopez-de Silanes, 1997, cited in Pennings, 2008; Vickers & Yarrow, 1988).

(ii) The view of property rights theorists (that focus on the principal-agent relation) that better manager incentives are fundamental in improving company performance. This view also has applicability under government ownership, according to various theorists (see, for example, Bardhan & Roemer, 1992, cited in Chang *et al*., 2003).

(iii) The neo-classical perspective that organisational weaknesses further account for poorer company performance under government ownership, namely: (a) lack of management autonomy; (b) internal inefficiencies in bureaucracies; and

(c) multiple and contradictory government objectives (cited in Vickers & Yarrow, 1988; Cook & Kirkpatrick, 2000a).

(iv) The neo-classical view that superior monitoring and control of managers under private ownership, because of capital markets and the takeover constraints that operate in the private sector, which are absent under government ownership, also account for the poorer performance of SOEs (Vickers & Yarrow, 1988; Cook & Kirkpatrick, 2000a). The applicability of counter-arguments that uncompetitive markets curtail better monitoring and control of private companies in developing countries is also briefly assessed against the mining sector (see, for example, Craig, 1991, cited in Cook & Kirkpatrick, 2000b).

(v) The argument that sustainable improvements in the standard of living and the welfare outcome, including economic growth, distribution and poverty effects of privatisation, in lower-income economies may not necessarily be positive in the long run, as private enterprises tend to neglect the economic, political and social consequences of their activities (Kiken, 1998, cited in Kirkpatrick & Parker, 2005; Cook & Kirkpatrick, 2000b).

The third research question in the mining sector case study regarding the roles of TNCs within a weak state and the development outcomes, is analysed by testing the validity of various theoretical arguments of both pro-TNC theorists (neo-classical and neo-fundamentalist) and anti-TNC theorists (Global Reach and neo-imperialist theorists), against observed events in the mining sector of Zambia. These entail an assessment of both the neo-classical (Vernon, 1979; Buckley & Casson, 1985) and neo-fundamentalists' (Warren, 1980) views that TNCs play a pivotal role in supplementing the capital and technology of the host country and of the counter-perspective of the Global Reach and neo-imperialist theorists (Lenin, 1917; Helleiner, 1989) that TNCs drain the resources and undermine the development of the host country (cited in Jenkins, 1987:27, 28).

In addition to such capital and technological contributions, the third research question further assesses whether the returns to Zambia from mining TNCs were optimal.

Optimal returns are crucial for ensuring more favourable outcomes in the case of exhaustible resources, according to various theorists. Exhaustible resources require an adequate capturing of rent by the government and the reinvestment of the capital allowance component in alternative forms of capital assets, to promote national development and to maximise long-term revenue (Blignaut & Hassan, 2002).

Moreover, the roles of the government in its relationship with TNCs in the Zambian mining sector are analysed against government measures considered by various theorists as necessary to attract TNCs and in guiding the activities of TNCs to more advantageous outcomes for the host country. The government's role is further assessed through its bargaining leverage compared to those of mining TNCs. Mining sector activities, which demand high technological and capital requirements and where the rent element is expected to collect major returns, require strong government bargaining skills to ensure that the greatest possible share of the rent element accrues to the host country (Chang, 1998:238). Developmental theorists consider a strong government bargaining leverage (a corporatist role) against TNCs as pivotal also to enable the government to direct the activities of TNCs to more favourable outcomes.

The locational decisions of TNCs are assessed through views of neo-classical theorists that unrestricted trade and industrial policies are crucial for attracting TNCs (Rugman, 1981, cited in Jenkins, 1987). These decisions are further examined against the counter-arguments that restrictive government policies, as long as they are not excessive but remain stable and predictable, are not significant in determining the locational decisions of TNCs (Chang, 1998).

The fourth question, pertaining to the capacity of the state in ensuring positive outcomes for the host countries, also in its relationship with mining TNCs, draws heavily on theories of the developmental state. Developmental theorists favour a greater interventionist role of the state, while neo-classical theorists favour a minimalist role. The capacity of the government in the mining sector is evaluated alongside certain criteria identified by Leftwich (1995), Chang (1998) and Amsden (1989, 1997) as important in enhancing the capacity of development states (although confined to those that have relevance to Zambia's mining sector). Such an evaluation involves a deductive use of theory which aids analyses of the Zambian state. The bargaining leverage of the government and the debate whether a minimalist or an interventionist role of the state is the better option in its relation with TNCs are important sub-elements in the assessment of the capacity of the state.

Finally, the question pertaining to the influences of different government mining policies and of the activities of mining TNCs on the political economy of Zambia mainly tests the validity of the neo-classical argument that a minimalist role of the state is necessary to attain higher economic growth. The contrasting views of Fine and Stoneman (1996) that minimalist government policies are not neutral are also examined against the case study. These theorists further argue that minimalist policies, subsumed in liberal policies and favoured by the International Monetary Fund (IMF) and the World Bank, have especially benefited private capital.

In addition, the research question tests the applicability of the argument of Bond and Manyanya (2002) that an increasing acceptance of IMF and World Bank policies, together with corrupt practices, signifies a realignment of the government away from the more marginalised, including workers, towards alliances with those that would assist them to remain in power. These policies especially favour foreign capital and the government elite over the workers, according to these theorists. The various theoretical arguments and literature reviews employed in the study are detailed in Chapter 3.

1.1.6 Contributions of the study

The study contributes to a greater understanding of the privatisation process of the Zambian mining sector during the transition from majority state ownership to private ownership. Such an investigation has not been comprehensively assessed because of the novelty of the privatisation process, with the mines only being fully privatised in 2000. Moreover, an unravelling of the costs and advantages of private ownership of the mines and of the roles of mining TNCs, in the context of a weak state, a liberalised economy, and powerful actors, contributes towards greater knowledge in these areas. Such an understanding also has wider application from which other developing countries, in particular African countries with comparable contextual realities and faced with the prospect of having to privatise their SOEs to TNCs, could draw. Empirical studies on the social aspects and on the impact of privatisation in sub-Saharan countries have largely been overlooked, owing to tendencies to focus on privatisation transactions rather than sector reorganisation, including wider social objectives (Buchs, 2003:1, 40).

The study further identifies the consequences arising from a poorly planned privatisation process. The identification of the preconditions for enabling more advantageous consequences for Zambia from the privatisation process and from the activities of TNCs could also serve as a reference from which other developing countries could draw to ensure more favourable outcomes from privatisation policies and from the activities of TNCs in their countries. Additionally, the illumination of the political-economic consequences of the privatisation policies and of the activities of TNCs in the mining sector in Zambia that would likely replicate in other African countries, with weak states, could play an important role in aiding policy formulation in these countries.

1.2 CONTEXT OF THE MINING SECTOR IN ZAMBIA

The Kaunda administration, governing Zambia under the banner of the United National Independence Party (UNIP) from 1964 to 1991, nationalised the copper mines in 1969. However, management control of the mines remained with the two private mining TNCs that had also enjoyed ownership of the mines before independence, namely Anglo American and Roan Selection Trust, until 1973. After 1973, management control of the mines by the state was introduced. Subsequent to the nationalisation of the mines in 1969, the Kaunda government had adopted strong interventionist policies.

The copper mines were not nationalised outright. The government initially took over ownership of only 51% of the mines and at the point of privatisation, the copper mining conglomerate, the Zambia Consolidated Copper Mines (ZCCM), still comprised of a combination of state and private interests. Section 4.2.1 of Chapter 4 provides a full explanation of the shareholding structure of the mining sector under government ownership of the mines. Accordingly, the economy for most of Kaunda's rule could more accurately be described as mixed, with a strong state presence. Government mining policies and the influence of multilateral institutions, such as the IMF and World Bank, also had a significant impact on the development of the mining sector and the Zambian economy.

The Chiluba government, which came into power at the end of 1991 under the Movement for Multiparty Democracy (MMD), embraced the full-scale neo-liberal policies prescribed by the IMF and the World Bank in the 1990s and implemented these policies more rigorously than the Kaunda government. The policies caused major changes in the operations and the political economy of the mining sector. The neo-liberal policies continued under the MMD platform, for the period of Mwanawasa's rule.

During Chiluba's government, majority private ownership of the mines by foreign companies was fully instituted in 2000 (Fraser & Lungu, 2007:54). The privatisation of the ZCCM entailed the breaking up or unbundling of the ZCCM (then one of the five largest copper-producing companies in the world), dividing its operating assets into packages and advertising each of these packages for sale (Craig, 2002:364). However, a long delay occurred from the passing of the Privatisation Act in 1992 (that sanctioned the privatisation of state assets in Zambia) and the privatisation of the ZCCM,[3] which commenced in 1997 and was only completed in March 2000 (Kaunda, 2002:27; World Bank, 2002a:4; Craig, 2002:Endnote 1:364; ZPA, 2000b:15). Table 1.1 summarises in greater detail and in chronological order, the various economic policies that the Zambian governments adopted for the period under investigation.

[3] A parastatal conglomerate that specialised in mining and in the processing of copper and cobalt.

Table 1.1: Chronology of changes in economic policies in the mining sector of Zambia

Independence (1964-69)	Accommodation period: mining remains under the control and management of TNCs
1969-73	State majority ownership but continued TNC management of the mines
1973 – December 1982	Centralised planning and controlled regime
December 1982 – October 1985	Decontrol and deregulation
October 1985 – April 1987	Considerably liberalised regime
May 1987 – November 1988	Return to controlled regime under the New Economic Reform Policies (NERP)
November 1988 – June 1989	Relaxation of some controls
July 1989 – September 1991	Return to a highly flexible regime, with movement towards full-scale liberalisation
October 1991	President Chiluba's MMD government took over power from the UNIP government of President Kaunda, through elections
November 1991 – 2001	Fully-fledged structural adjustment programme and stabilisation measures
2002-08	Continuation of Chiluba's neo-liberal policies during President Mwanawasa's rule, also under the MMD platform

Source: Adapted from Saasa (1996:45).

On a macro-economic level, the strategic significance of the copper mining sector in Zambia resides chiefly in its role as the major contributor to Zambia's foreign exchange earnings. Mining (mainly copper mining that accounted for 96.5% of total mining exports in 1987) has for the most part consistently contributed over 90% of Zambia's exports until the mid-1990s (The Economist Intelligence Unit, 2002:27; World Bank, 2004a:48; Saasa, 1987:7). From independence to the mid-1970s, mining further contributed significantly to the gross domestic product (GDP) of the country.

The role of Zambia, as a leading producer of unrefined copper, in the late 1960s, greatly assisted towards establishing the country as one of the most developed and urbanised countries on the continent in the 1970s during Kaunda's government. However, the economic growth trends subsequently lost momentum and declined over the following decades (Van Buren, 2003:1152; The Economist, 2002b:1; Maambo, 1998:Fig. 1; World Bank 1996:1, 2002a:4, 2003b:134). Moreover, the country's high dependence on the mining sector, a non-renewable resource, accounts for the poor diversity or the weak development of the rest of the Zambian economy. It also renders the Zambian economy highly vulnerable to the price of copper.

The significant drop in the price of copper in the mid-1970s contributed to the considerable decline in the contribution of mining to GDP and to a chain of negative influences on the Zambian economy. Copper production fell and the consequent high balance of payment deficits led the Zambian economy into debt, forcing the government to seek lending from the IMF and the World Bank. Subsequently, for most of the 1980s, the Zambian government was forced to adopt Structural Adjustment Programmes (SAPs) from the IMF and the World Bank, entailing more liberal policies.

Most notably in the 1990s, a significant decline took place in the mining sector's contribution to the Zambian economy, namely its contribution to GDP, employment and to government revenue. This was also the case in the short term, under private ownership of the mines. Under private ownership of the mines, the most important contribution of the mining sector to the Zambian economy continues to subsist in its dominance as the major foreign exchange earner in the country, albeit at a lower level than during Kaunda's government. Moreover, a visible trend under private ownership of the mines, especially prior to the copper price boom, was the conspicuously poorer contribution of mining to government revenue, than under government ownership of the mines immediately before the mines were privatised.

Although copper mining under private ownership seems unlikely under the present conditions to continue dominating the economic development of Zambia in the long term, it is nevertheless likely to remain important in the short to medium term. This is because a closure of the mining sector would have a devastating socio-political and economic effect on the country.[4] Also, in the absence of significant improvements in the development of other sectors, a more effective performance of Zambia's mining sector remains crucial to the development of the economy.

1.3 CHAPTER OUTLINE

Chapter One presents an introduction to the study. The research methodology of the study is discussed in Chapter Two. The literature reviews and theoretical frameworks employed to guide analyses in the study are expounded upon in Chapter Three. Chapter Four provides background information of the Zambian mining sector. This encompasses an overview of the Zambian economy; the policies of the Kaunda and the Chiluba governments and of the IMF and the World Bank that affected the mining sector; the political-economic implications of government policies; and an assessment of various economic indicators. Chapter Five evaluates the privatisation of the mining sector and the impact of changing ownership and management structure on the economy. Chapter Six considers the roles of TNCs in the mining sector in Zambia within a weak state. Chapter Seven presents a summary, recommendations as well as concluding remarks of the study.

[4] Interview with M. Shandavu, 10 October 2003.

CHAPTER 2

2. RESEARCH METHODOLOGY

The research methodology elaborates on the research methods and the limitations of the methodology of the study.

2.1 RESEARCH METHODS

The research methods outline the research approach, the techniques employed in the study, the roles of theory and data, the nature of the data and the research strategy.

2.1.1 Research approach

The research adopts a case study approach. A case study approach is the most appropriate method to explore rather novel events. These include the privatisation process of the copper mines, the roles of significant actors, especially the state and the mining TNCs in the mining sector of Zambia and the development and political-economic impact of the changes in policies and actions of different actors on the copper mines. The mines in Zambia were fully privatised only in 2000 and the consequences of the privatisation of the mines to TNCs are as yet not well documented. The case study approach also enables a greater understanding of the various factors that relate to the core research issues and their impact on the development of the mining sector.

2.1.2 Techniques

The predominant techniques employed in the study involve literature research and fieldwork. Moreover, the study principally adopted a qualitative approach, rather than a statistical analysis of causality. The statistics employed in the research serve mainly to *describe* the various issues and trends under consideration. A further technique used in the study is a triangulation technique entailing a combination of various data collection techniques, which overlap to investigate the same issues.

The fieldwork was pursued mainly to gain information on more recent events affecting the mining sector in Zambia. The information was gathered to obtain greater insight mainly on the research questions relating to the privatisation of the mines, the operations of the mines under private ownership and the roles of TNCs in the mines, which are also not yet well documented. The fieldwork involved in-depth interviews of persons with expert knowledge on the various issues, especially those pertaining to the more recent period. Sixty people were interviewed for the study.

The officials that were interviewed in Zambia were from the Ministry of Mines and Mineral Development, the Ministry of Finance and Economic Development, the Ministry of Commerce Trade and Industry, the Bank of Zambia (BoZ), the Mineworkers Union of Zambia (MUZ), the IMF, the World Bank, the Zambia Association of Chamber of Commerce and Industry (ZACCI), academics, journalists and senior personnel of mining TNCs. An official from the Industrial Development Corporation (IDC) was interviewed in South Africa. Some interviews were also conducted at the end of 2001, as part of a study for the Sociology Department of the University of the Witwatersrand, to obtain background knowledge of more current events. The list of people that were interviewed is detailed in the Table attached to the Reference section.

Different questions were generally employed for interviewing the various officials, focusing largely on their areas of expertise. However, the same questions were also at times posed to different officials, enabling the cross-referencing of information and improving the reliability of information. In instances where opinions were given, additional and more objective information (from statistics, literature and newspapers etc.) was sought to check their accuracy. The interviews were audio-recorded and transcribed verbatim.

2.1.3 The role of theory

The appropriate theoretical arguments are principally employed to map out avenues against which the various issues under investigation are analysed. As such, the theory guides the analyses of the study. The analytical approach is largely exploratory in nature, in that the theories are treated mainly as ‘preformulated questions’ (indicating feasible avenues of explanation), rather than as ‘preformulated answers’ (suggesting well-defined specific hypotheses) (Wuyts, 1992:13). Accordingly, the role of theory in the study is to provide guidance as well as to raise questions concerning the issues under consideration, which are then followed up with the analyses of data.

2.1.4 The role of data and empirical evidence

Rather than testing for well-defined specific hypotheses, the different theories are compared in the study against actual evidence that enable the extraction of *plausible* theoretical explanations. This is accomplished through the elimination of implausible explanations, while retaining those that constitute possible explanations for the issues under investigation (Wuyts, 1992:4). Accordingly, data analyses and empirical evidence serve as means against which the plausibility of competing theories are compared and evaluated. This process contributes towards improving existing theories.

2.1.5 Nature of data

The statistical data employed in the study were largely obtained from secondary sources, principally through published statistics from Zambia's Central Statistics Office, the BoZ, the World Bank, the IMF and The Economist Intelligence Unit. Most of the information supplied by the BoZ was obtained from the Zambian Central Statistical Office. Other information was acquired from literature and the more recent information that is not well recorded in the literature was in a few instances obtained from primary sources, especially through interviews.

2.1.6 Research strategy

The research strategy employed for analysing the research encompasses, as a starting point, the development of a theoretical framework, achieved through comparing various appropriate complementary and rival theories. The comparison enables the identification of different views on the problem and the exposure of loose ends of the different theories, which improve the explanatory depth of the issues under consideration. Subsequently, the data and empirical evidence are analysed by way of constantly testing them against appropriate literature and theoretical arguments for the different issues under consideration, which facilitate the identification of more plausible explanations of the theories. The philosophical foundation of this method of analysis is 'the principle of inference to the best explanation', entailing the inferring of hypotheses (or preformulated questions in the case of the study) that correctly provide the best explanation for the available evidence (Wuyts, 1992:4-5).

An inductive approach is largely employed in the study, through the process of eliminating those aspects of theory that are considered implausible in explaining events, while retaining those that provide a more plausible explanation. In this way, the data and empirical evidence contribute to theory building. Also, since theory is not considered in the study to offer definitive answers but to provide only *possible* conclusions to be tested against empirical evidence, the approach of the study is largely positivist, rather than rationalist. The inductive approach employed in the study in particular encompasses the testing of issues, drawn from the theoretical perspectives and literature reviews on privatisation and private- and state-owned enterprises, the roles of TNCs and the roles of the state and the market, against the Zambian mining sector.

A deductive method involving the use of certain theoretical criteria as the standard, against which actual events are compared is also employed, but to a lesser extent. The deductive method is mainly utilised to enable an evaluation of government policies against the preconditions several theorists consider pivotal for ensuring more beneficial privatisation and activities of TNCs in developing countries. A deductive method is also employed to assist analysis of the capacity of the Zambian government.

2.2 LIMITATIONS OF THE METHODOLOGY

Notable weaknesses of the methodology entail the possible shortcomings and inaccuracies of certain statistical data. The inaccuracies and shortcomings arise from the fact that statisticians of national income accounting in many developing countries often having to resort to intelligent guesswork to fill the gaps and because of difficulties in obtaining statistical information as a continuous series for the period under investigation (1964 to 2006/7), especially for the earlier years. Significant weaknesses also exist in more recent national statistics from the 1990s, reflected in the major discrepancies between official figures and those of multilateral institutions such as the IMF and the World Bank.

In particular, the non-monetary statistics of the BoZ are questionable. Accordingly, rather than employing statistics only from the Central Statistics Office (CSO) and from the BoZ, several other sources of information were also used in instances where the official figures appeared to be inaccurate. The study relies heavily on the Economist Intelligence Unit for several sets of data. Allowances should therefore be made for inaccuracies that occurred as a consequence of possible statistical imprecision at the source or from having to switch to different sources to fill the gaps.

More specifically, data on GDP by expenditure and of the balance of payments possibly have shortcomings, owing to inadequate methodology and unreliable data sources in Zambia. Imports from Zimbabwe were under-reported, with official figures likely to capture less than half the total (The Economist Intelligence Unit, 2007b:42, 49, 2008b:25). Moreover, official GDP growth data fail to adequately capture the activities of smaller sectors, such as wholesale and retail, trade and business services (The Economist Intelligence Unit, 2008b:25).

The sectoral contribution from 1989 to 1994 also varies greatly among different sources. Furthermore, while the IMF and the Economist Intelligence Unit disaggregated the contribution of mining and of manufacturing to GDP before the 1990s, these were subsequently lumped together under the 'contribution of industry to GDP', making it difficult to disaggregate the trends in the contribution of mining and manufacturing to GDP. The national statistics further do not capture structural changes in the economy, since calculations of the data are still based on 1994 weightings (The Economist Intelligence Unit, 2007b:49, 2008b:25).[5] While the official monetary data correspond fairly closely to the IMF figures, these are often substantially revised and not published

[5] However, a new economic census is currently under way (The Economist Intelligence Unit, 2008b:25).

elsewhere, other than the monthly fiscal data provided to the IMF (The Economist Intelligence Unit, 2008b:25).

In addition, although the mining companies provide annual or periodic reports to the Mines Safety Department, the Ministry of Mines, the Zambia Revenue Authority (ZRA), the BoZ and the Environmental Council of Zambia (ECZ) and others, these reports are not publicly accessible (Fraser & Lungu, 2007:17). Furthermore, the investment, employment and profit figures for some of the firms are not recorded clearly in annual reports, and the data on contributions to national tax from each of the mining companies are difficult to obtain. An assessment of the performance of the mining sector, based on profit, was therefore not possible within the scope of the study.

Problems encountered during the fieldwork in Zambia encompassed frequent cancellation and postponement of pre-arranged interviews that tended to be the rule rather than the exception. Managers at Konkola Copper Mines (KCM), under government majority ownership, following Anglo American's departure, also cancelled pre-arranged interviews on the basis that the interviews might jeopardise the sale of the company. Moreover, officials mostly neglected to respond to queries concerning discrepancies or likely inaccuracies in the statistics. However, since the statistics are largely used for descriptive, rather than for analytical econometric purposes, minor imprecisions are unlikely to significantly influence the accuracy of interpretations. Furthermore, since the privatisation of the mines was only completed in 2000, the longer-term effects of the privatisation and private ownership of the mines by the TNCs on the economy have not as yet played out and are difficult to predict because of the influences of various variables, not least the international demand for copper, on the development of the mining sector.

CHAPTER 3

3. LITERATURE REVIEW AND THEORETICAL FRAMEWORK

The main groups of theoretical arguments and literature reviews drawn on to address the research questions are: (i) privatisation and private and state ownership of enterprises; (ii) the roles of TNCs; and (iii) the roles of the state.

3.1 THEORETICAL PERSPECTIVE ON PRIVATISATION AND PRIVATE AND STATE-OWNED ENTERPRISES

Privatisation involves the transfer of ownership of SOEs from the public to the private sector; often termed divestiture[6] or denationalisation (Cook & Kirkpatrick, 2000a:220; Low, 1991:1). The theoretical investigation of privatisation and private and state ownership firstly entails an evaluation of the privatisation of SOEs and of private and state ownership. This is followed by a consideration of the preconditions for ensuring a more successful privatisation.

3.1.1 Evaluation of the privatisation of SOEs and of state and private ownership

Pro-privatisation proponents ascribe two central advantages to the privatisation and the private ownership of SOEs. These include:

i. An augmentation of government revenue from the sales of the SOEs, from taxing private companies and from the elimination of state subsidies that would, by reducing fiscal imbalance, improve public finances (public finance effect).
ii. Improvements in the performance of the company, partly owing to greater *x*-efficiency objectives of private companies (Pinheiro, Buchs, Kayizzi-Mugerwa, Adam, *et al*., 1992, cited in Bova, 2009:4; World Bank, 1992, cited in Cook & Kirkpatrick, 2000b:8).

(i) Increases in government revenue

The argument of the pro-privatisation proponents, also of the World Bank, that privatisation would increase government revenue and subsequently improve the fiscal imbalance, is not invariably correct. For example, in sub-Saharan Africa, government

[6] Divestiture is more narrowly concerned with the sale of equity or assets of (SOEs) as well as the outright liquidation of enterprises as legal entities (Bennell, 1997:1786).

budgets received only a fraction of the proceeds from privatisation and the contributions of the proceeds to the budget were, in some instances, wiped out. Moreover, the effects of privatisation in these countries tend to be confined more to a damage-limitation exercise, rather than an economic booster. The poor gains were mainly owing to proceeds being channelled, by law, to extra-budgetary funds to finance specific activities or operations, such as settling liabilities and retrenchment or severance payment costs (Buchs, 2003:11, 12, 40, 41).

Increases in government revenue from privatisation would also significantly depend on the sale price of the SOEs (Cook & Kirkpatrick, 2000a:221; Pennings, 2008:484). If the SOE is sold at a price below the net income flow[7] that the enterprise would have created if it remained in the public sector, without reform, in the long run, the state will gain financially only if it obtains sufficient tax payments from the newly privatised enterprises (Buchs, 2003:12, 13; Cook & Kirkpatrick, 2000a:221). The auction design is also important in determining government revenue from privatisation (Pennings, 2008:484).

For instance, higher government revenue would be obtained when the privatisation involves a cash-only bid over pledged investment. However, compulsory investment and retained shareholding by the government, if both are announced before the auction, would also hold considerable benefits for the government (Pennings, 2008:489). Cash payments would however have limited benefits if corrupt practices are involved in the privatisation process. As the winners of the privatisation process are likely to transfer money to safe havens, especially when deep depressions contribute to low returns, or when large-scale corruption was involved in the privatisation process, resources might also leave the country (Stiglitz, 2002:144).

Under private ownership, an increase in government tax revenue from private enterprises will depend on the level of pre-privatisation subsidisation and on the overall efficiency of the tax system (Buchs, 2003:13). Moreover, higher profitability and

[7] Some SOEs are sold well below the maximum that rational private buyers would offer, partly due to incorrect financial records, to speed up the process, or due to a wish to subsidise the private sector (Cook and Kirkpatrick, 2000b:23).

efficiency at private firm level may not necessarily translate into improved tax revenue. Tax evasion tactics of private firms and weaker tax administration of the government under private ownership, pertaining to several sub-Saharan countries, may lower tax revenue. Privatisation has been less decisive than profound tax administration reform for revenue performance (Buchs, 2003:12, 13). Potential tax revenue under private ownership would further be eroded if the new private owners receive benefits, such as tax deductions, duty free imports, tariff protection and priority access to credit and other scarce inputs (World Bank, cited in Cook & Kirkpatrick, 2000b:20, 21).

(ii) Performance improvement of companies

Dominant factors that neo-classical theorists attribute to the superior performance of private companies over SOEs, assessed below, are: (i) the different performance objectives of respective principals (the owner, recipient of dividends, or a shareholder of residual profits); (ii) the superior incentive arrangements and control of managers under private ownership; and (iii) greater weaknesses in the organisational structures of SOEs over private companies (Vickers & Yarrow, 1988:7, 36).

- *Objectives of principals*

The different interests of the shareholders and of the wider public, the respective principals of private- and state-owned firms, force agents (managers) of private and public enterprises to promote dissimilar economic outcomes, according to neo-classical theorists. At times, managers in SOEs also serve the interests of government departments for which they are responsible, in which case the government is the principal (Vickers & Yarrow, 1988:7). The government, as an agent of the wider public, in their dealings with industry, pursues electoral-maximising motives over profit-maximising and cost-reduction objectives. In pursuing the interests of its voters, the government is encouraged to maximise economic welfare objectives, by way of maximising allocative efficiency (whereby the output level of the firm is maximised at a socially optimal level, within a given cost structure) but limits enterprise efficiency.[8] This is in line with public interest theory (Vickers & Yarrow, 1988:8, 27, 36).

[8] Which is defined by some form of welfare function (the sum of consumers' and producers' surpluses).

On the other hand, privatisation involves a change in both the principals' objectives from welfare maximisation to profit maximisation. Profit-maximisation objectives under private ownership are achieved through greater internal or *x*-efficiency motives of private companies, over SOEs that are considered as invariably inefficient, according to neo-classical theorists. *X*-efficiency implies a lower total cost of production for a given output level (Cook & Kirkpatrick, 2000b:20, 21).

Company performance would, therefore, improve under private ownership, mainly owing to more efficient use of an asset than under government ownership (Lopez-de Silanes, 1997, cited in Pennings, 2008:489). Accordingly, ownership matters in determining company performance, in the view of neo-classical theorists (Commander & Killick, 1988, cited in Cook & Kirkpatrick, 2000b:22). Privatisation would, though, affect a fall in output, since the government no longer subsidises the newly privatised firm to maintain inefficiently high output levels, according to Boycho *et al*. (1993, cited in Boubakhri & Cosset, 1999:20). However, in the case of mining resources, where the price is determined on the London Metal Exchange (LME), the role of the government in sustaining high production levels is less clear than the case with the utility sectors.

Some theorists argue that theoretical and empirical evidence that SOEs are pervasively inefficient, by virtue of ownership *per se*, are unconvincing (Millward, 1988:157, cited in Cook & Kirkpatrick, 2000a:219; Chang & Singh, 1992:42, cited in Cook & Kirkpatrick, 2000b:24). Depending on the effectiveness of the state as an agent and principal, SOEs may not necessarily be inefficient. For instance, in South Korea and Kenya, SOEs achieved significant profitability and efficiency and were sustained for lengthy periods (Song, 1993; Grosh, 1992, cited in Cook & Kirkpatrick, 2000b:24).

Moreover, privatisation *per se* would not automatically promote greater *x*-efficiency; and the conditions under which privatisation can achieve efficiency and equity are very limited, according to Sappington and Stiglitz (cited in Stiglitz, 1998:19). On the contrary, when privatisation occurs with capital market liberalisation,[9] rather than enhancing efficiency, growth and re-investment in the country, the incentive for corporate theft and asset stripping by insiders increases (in particular, when new firms are uncertain of their future). In such instances, growth might, in fact, be depressed. Local governments also have the incentive to strip the assets of newly privatised firms (Stiglitz, 2002:144, 155, 157, 158). Furthermore, regulatory reforms in transition economies in Eastern and Central Europe seem less an instrument of promoting efficiency and competition than a means for attracting private investment, by ensuring through regulation that private firms make an adequate return on their capital (Cook & Kirkpatrick, 2000b:18).

Enterprise performance also needs to be viewed in the broader context, taking into account the economic, social and political reforms and of long-term sustainable improvements in the standard of living and the welfare of the country (Cook & Kirkpatrick, 2000b:24). The social aspects of privatisation have largely been overlooked in sub-Saharan Africa, primarily due to the tendency to focus on privatisation transactions, rather than sector reorganisation, including social objectives (Buchs, 2003:40). Additionally, foreign ownership may be politically, economically and socially destabilising (Kirkpatrick & Parker, 2005:531). Accordingly, the welfare outcome of privatisation in a lower-income economy, in particular economic growth and the distribution of wealth and the poverty effects, is uncertain (Kikeri, 1998, cited in Kirkpatrick & Parker, 2005:529).

Furthermore, efficiency may be improved at the cost of employment, as was the case with the Soviet Union in the 1990s. The GDP of that country also fell by 54% and industrial production declined by almost 60% between 1990 and 1999 (Kemal, 1993, cited in Cook & Kirkpatrick, 2000b:21; Stiglitz, 2002:143). The decline in the GDP of the Soviet Union challenges the argument of pro-privatisation proponents that privatisation is expected to benefit growth by raising the returns to private capital accumulation (Stiglitz, 2002:143). Accordingly, overall efficiency, which is only

[9] Especially when an effective legal infrastructure to ensure good governance is absent.

possible if workers move from low-productivity jobs to high-productivity employment, might not always materialise with privatisation (Stiglitz, 2002:143).

In cases where privatisation has failed to achieve economic efficiency or if the quality of human capital is adversely affected, for instance through reduced training and worker health, it would hinder growth (see, for example, Pineda & Rodriguez, 2002, cited in Kirkpatrick & Parker, 2005:528). The negative impact of privatisation on some services and on net employment likely affected mainly the middle-lower income groups in sub-Saharan countries (Buchs, 2003:40). However, the reduction in employment might have been necessary in sub-Saharan Africa as a damage control exercise and because SOEs are usually overstaffed (Buchs, 2003:21). Also, in growing sectors, the newly privatised firms could absorb surplus labour through new capital investment and more productive use of existing assets (Hikery, Nellis & Shirley, 1992, cited in Boubakri *et al*., 1999:28).

- *Incentives*

In addition to the stronger profit-maximisation objectives of their principals and property rights, the superior incentives that principals provide to agents in private companies, over SOEs, also account for the better performance of private enterprises, according to neo-classical theorists (Vickers & Yarrow, 1988:7; Cook & Kirkpatrick, 2000a:217). This is accomplished through the superior incentives ensuring a more effective principal-agent relation, by way of encouraging a modification of manager behaviour to align more closely to the objectives of the principal, namely, to strive for performance improvements (Cook & Kirkpatrick, 2000a:217; Low, 1991:27). In particular, property rights theorists, who reject profit-maximisation as the behavioural guide, place the emphasis more on the principal-agent relationship than on ownership, in determining company performance (Low, 1991:27). In their view, managers, rather than owners, pursue their own interests in firms. Incentives provided to managers of private firms considered to promote profit-maximising objectives, include the linking of rewards for manager performance to the companies' share prices, via share ownership, or option schemes (Vickers & Yarrow, 1988:7).

The contention as to the relative importance of the two arrangements, viz. incentives or ownership, in improving efficiency has led various theorists to argue that privatisation is not the only way of handling incentives and agency problems in the management of public firms. Rather, since managerial incentives do not pertain exclusively to private ownership but could also be directed to state managers to improve efficiency in SOEs, other types of incentives or the creation of effective incentives would improve efficiency under any type of ownership and are not exclusive to private ownership (Cook & Kirkpatrick, 2000a:210, 2000b:24). The favourable outcomes of industrial reforms in China, as opposed to the poor performance of the Soviet Union under private ownership, are often used to support the argument that the privatisation would not necessarily result in improved enterprise efficiency, especially when widespread imperfections exist (Jefferson & Rawski, 1994:64; Lin *et al*., 1996, cited in Chang, McCall & Wang, 2003:416).

Greater management autonomy, while the government still maintains overall control, is considered by some theorists as a sufficient incentive for socialist firms to become as efficient as their capitalist counterparts (Bardhan & Roemer, 1992:102, cited in Chang *et al*., 2003:415). Corporatisation of public firms[10] in New Zealand and the reforms of large SOEs in Poland have had a positive influence on their performance (Hume & Pinto, 1993, cited in Cook & Kirkpatrick, 2000b:24). In contrast, other theorists argue that ownership and control rights matter and have significant efficiency implications (Grossman & Hart, 1986; Hart & Moore, 1990, cited in Chang *et al*., 2003:415). The argument is somewhat supported by an empirical study on China's Township and Village Enterprises (TVEs), showing that management incentive contracts have positive but a less significant impact on efficiency, over well-defined stock-based ownership rights (Chang *et al*., 2003:426).[11] However, more studies are necessary to investigate the effects of alternatives to total privatisation.

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[10] Essentially involving a reorganising of a government body into a company that would still be owned by the government but the corporatised entity would be subjected to the discipline of the marketplace, encompassing also a more streamlined and responsive civil service (Low, 1991:188, 189).

[11] This was the case even during the transition period when market-supporting institutions were still developing.

Under state control with performance contracts, the lack of financial discipline and performance accountability may undermine the efficiency of enterprises (Bennell, 1997:1800). Reforms of SOEs, through performance contracts, require commitment by both parties, some recapitalisation of the enterprise, enforceable targets, incentives and censure or financial punishment in the event of poor performance that are not always easily achievable (World Bank, 1994, cited in Bennell, 1997:1800). SOEs would nevertheless be desirable over private firms, in instances involving 'strategic' activities (activities possessing strong positive externalities, such as technological development, labour training and public health provision)[12] in competitive markets (Cook & Kirkpatrick, 2000a:211-212).

Furthermore, since improvements in the performance of enterprises are also dependent on factors other than ownership, an assessment of the differences in the performance of firms based solely on ownership is simplistic and highly misleading, according to empirical studies on the relative performance of public and private industries in the UK (Vickers & Yarrow, 1988:8, 9). A complex of additional contributing factors, besides ownership, also influences management incentive structure and economic performance. These factors include the age, scale and technological progressiveness of the industry, market structure,[13] organisation, institution building (including forms of external regulation)[14] and political economy (Cook & Kirkpatrick, 2000a:211; Chang & Singh, 1992:54, cited in Cook & Kirkpatrick, 2000b:24).

- *The monitoring and control of managers*

Less effective monitoring and control of managers by the principals under state ownership over private ownership of companies are further responsible for the poorer performance of SOEs in comparison with that of private firms, in the view of property rights theorists. This is because the less effective monitoring and control of managers contribute to public managers being less motivated to maximise the value of the assets of public enterprises (Hanke, 1986:16, cited in Low, 1991:27; Cook & Kirkpatrick,

[12] Private firms would be unable to recover the full social benefits created by such activities.
[13] Or the degree of competition in the market.
[14] Include the effectiveness of monitoring systems, which is influenced by the availability of the relevant institutional environment.

2000a:210). Constraints on managers pursuing their own objectives or interests and on poor financial performance under private ownership include shareholder monitoring and the possibility of takeovers if firms perform badly, and of bankruptcy in the case of default (Vickers & Yarrow, 1988:11; Cook & Kirkpatrick, 2000a:210).

On the other hand, the absence of incentives under SOEs[15] and the lack of deterrents, such as a bankruptcy and takeover constraint (since SOEs, by nature, cannot be taken over) for poor financial performance preclude capital markets and the takeover constraints from being employed to promote and to control manager performance under public ownership (Cook & Kirkpatrick, 2000a:210; Vickers and Yarrow, 1988:27). Under government ownership, the diffusion of property rights among a large number of shareholders diminishes the incentive to individuals to incur the substantial information costs needed to monitor and control management and employees' behaviour in SOEs. In instances where control is exercised under state bureaucracy, the control is either weak or the objectives pursued may contradict enterprise efficiency, according to property rights theory. Moreover, it is argued that the roles of the state, often as both the principal and agent (since the government is both the manager and the recipient of dividends under state ownership), further reduce the effective control and monitoring of managers of SOEs, as compared to those of managers under private ownership (Cook & Kirkpatrick, 2000a:210).

The neo-classical argument that capital markets and the possibility of a takeover act as constraints to discipline poor management performance under private ownership may not necessarily operate in developing countries. The general absence of or the poor levels of competitiveness of capital markets, especially in developing countries, render them ineffective as regulators of manager performance within private firms in these countries (Craig, 1991, cited in Cook & Kirkpatrick, 2000b:17). Moreover, the rule of takeover (which encourages internal or manager efficiency) is considered to apply only to smaller firms that are more vulnerable than larger firms to takeover constraints. This implies that takeover threats cannot act as a reprimanding device against the manager

[15] By virtue of the government being both the owner and recipient of dividends.

inefficiencies of larger firms (Cook & Kirkpatrick, 2000a:210-211; Vickers & Yarrow, 1988:24).

- *Weaknesses within organisational structures of SOEs*

Weaknesses within organisational structures of SOEs represent an additional reason for the poorer performance and management of SOEs, according to pro-privatisation proponents. The weaknesses firstly include the lack of management autonomy[16] in government bureaucracies, since politicians tend to intervene directly in managerial decisions, which is likely to stifle decision-making (Cook & Kirkpatrick, 2000a:209, 216, 217; Low, 1991:25; Vickers & Yarrow, 1988:32). Secondly, internal inefficiencies in bureaucracies, such as inadequate staffing, especially at managerial level (the likely outcome of poor terms and conditions under state ownership), act as a disincentive for attracting capable managers, which also contribute to the poorer performance of SOEs (Cook & Kirkpatrick, 2000a:209). The private sector is considered as better able to attract and mobilise skilled talent than the government (Low, 1991:25). The above discussion nevertheless shows that incentives can also improve under SOEs.

A third weakness that pro-privatisation proponents ascribe to the poorer performance of SOEs relates to the multiple and contradictory government objectives. These objectives, forcing the government to trade off commercial profit and social objectives, render it difficult for the government to achieve both goals simultaneously, with commercial profits likely to suffer. Social objectives may also be displaced by political objectives under state ownership, according to neo-classical theorists. Fourthly, tendencies of corruption and nepotism under government ownership are further considered to undermine the performance of SOEs (Cook & Kirkpatrick, 2000a:209, 216, 217; Vickers & Yarrow, 1988:30, 34). However, the very privatisation that is often sold as a solution to the endemic corruption that plagues SOEs, has created new patronage opportunities in sub-Saharan Africa, suggesting that privatisation did not eliminate rents (Buchs, 2003:41).

[16] Which is necessary to take decisions in response to market opportunities.

3.1.2 Preconditions for more successful privatisation

Certain preconditions, often absent in developing countries, are necessary for privatisation to have a more positive impact on development. Privatisation is generally less successful in sub-Saharan countries, compared to that in the developed and East Asian countries (Cook & Kirkpatrick, 2000b:15). Kenneth Arrow's groundbreaking work on the dynamics of why and when market economies work and how economies change concludes that privatisation is secondary in importance to competition and the creation of an institutional infrastructure for a market economy (Stiglitz, 1998:19, 20, 2002:182). Competition is, however, not relevant in the case of the mining sector in Zambia, as the copper price is determined on the LME and foreign countries are the predominant consumers of Zambia's copper. Effective legal structures (covering contracts, bankruptcy and corporate governance) and institutional structures for strong corporate governance and corporate restructuring have great relevance (Stiglitz, 2002:157, 220).

Without adequate legal and institutional structures, the significant management autonomy and discretion that private companies possess would expose private firms to organisational challenges not dissimilar to those of public enterprises. The discretion that private companies possess is mainly on account of shareholders' lack of direct contact with the daily activities of the enterprise (similar to the legislature in public companies). Also, a World Bank study of transition economies shows that privatisation without effective institutional infrastructures for corporate governance has no positive effect on growth (Stiglitz, 2002:19, 20). Institutional transformations have been the weakest link in the reform agenda and undermined the credibility of privatisation in sub-Saharan Africa (Buchs, 2003:46). Enforcement problems have also greatly limited the effectiveness of institutions in sub-Saharan countries. Institution and capacity building need to be part of the reform agenda in a more systematic way in these countries (Buchs, 2003:1, 44).

Moreover, privatisation will gain greater legitimacy and would likely be more successful if measures are introduced to reduce its negative impact on the broader society, such as benefits to the unemployed and adjustment to pensions and salaries in line with inflation. These measures, together with the creation of an institutional infrastructure,[17] account to some extent for Poland's more effective market economy, compared to those of other East European countries (Stiglitz, 2002:181, 262). In the case of China the more successful transition was also as a result of the democratic support for reform and of the creation of institutional infrastructures such as an effective Securities and Exchange Commission, bank regulation and safety nets. This is an aspect to which the IMF gives insufficient consideration. Democratic support for the reforms in China was largely attained through the maintenance of social stability at the time that SOEs were downsized, through an avoidance of massive unemployment and through the creation of new jobs in tandem with restructuring[18] – viz. through 'creative destruction' (Stiglitz, 2002:183, 184).

Furthermore, the pace, sequencing and scope of privatisation and regulation are highly significant in enabling a more orderly restructuring. A rapid privatisation, or the 'shock therapy' that radical market reformers such as the IMF favour, would likely carry political costs that would hinder further reforms in the absence of effective legal and institutional structures (Stiglitz, 1998:19, 22). Insufficient regard for how privatisation was achieved and paying too little attention to the policy's social and distributional consequences have facilitated corruption and rampant inflation[19] and contributed to decreases in income and increases in inequality in Russia (Stiglitz, 2002:144, 157, 169). The greater success of China in the transition towards a market economy can be further attributed to a more gradual approach before privatisation was introduced, which allowed for the establishment of new enterprises and job creation, and a restructuring of the existing structures. A more gradual approach to privatisation enables better sequencing of reform and the creation of the prerequisites for good privatisation (Stiglitz, 2002:162, 184).

[17] Such as banks that lend, legal systems that can enforce contracts and a process of bankruptcies.
[18] Which involves the elimination of the old economy by creating a new one (Stiglitz, 2002:183).
[19] Which wiped out the savings of many countries.

3.2 THEORETICAL PERSPECTIVES ON THE ROLES OF TNCs

The term 'TNCs' refers to companies producing in more than one country and is not used in the study in the formal sense, as defined by Hirst and Thompson (1996:11).[20] The economic roles of mining TNCs and their relations with the governments of host countries are investigated using the arguments mainly of pro-TNC proponents (the neo-classical theorists and Marxist neo-fundamentalists) and of TNC critics (the Global Reach and Marxist neo-imperialist theorists – the latter include the dependency theorists), according to the categorisation of Jenkins (1987:17). Notwithstanding the dissimilar views on the ultimate outcome of TNCs' activities, the Marxist neo-fundamentalists support the neo-classical perspective that TNCs play a progressive role, especially in developing host countries. This perspective contrasts with the stance of non-Marxist Global Reach theorists (derived from Hymer's industrial organisation theory) and of Marxist neo-imperialist theorists that TNCs play a subversive role in these countries.

Mining sector activities, which demand high technological and capital requirements and where the rent element[21] is expected to collect major returns, require strong government bargaining skills to ensure that the greatest possible share of the rent element accrues to the host country (Chang, 1998:238). Nwoke defines mining rent as "the difference between the market price of a unit of mineral resource sold in the form of finished products and the total average costs incurred in discovering, producing, transporting, refining, and marketing the unit of that particular mineral resource. Total average costs are current costs, and a fair rate of return required by a private firm in the minerals industries" (Nwoke, 1984:42, cited in Ciccantell, Smith & Seidman, 2005:6, 7). Several theorists attribute the poor performance of especially African resource-rich economies to certain weaknesses in the governance of these countries, rather than to mining itself. This view suggests that the 'resource curse' argument promoted by some theorists,

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[20] According to their definition, TNCs are considered as truly global entities serving global markets through global operations with internationalised management and their locational decisions are motivated largely by where returns are highest and most secured. Accordingly, TNCs would not be based in one predominant national location (as with multinational companies) but are truly footloose without specific national identification and they are able to operate effectively independent of parent companies and unconstrained by the politics of particular nation states. Since this is not necessarily the case with the foreign mining companies in Zambia, the more appropriate term for these companies is 'multinational' rather than 'transnational companies'.

[21] Nwoke (1984) broadens Marx's concept of rent to the extraction of minerals in peripheral nations.

namely that resource-abundant countries display poor economic growth and development outcomes (see, for example, Sachs and Warner, 1997), needs not be inevitable.

Accordingly, key considerations in the theoretical debate on TNCs in the mining sector entail an examination of the contributions of TNCs to capital and technology, which are significant requirements in the mining sector. The returns to the local economy from the activities of TNCs in the mining sector are then investigated. This is followed by an examination of the roles of the government in ensuring more favourable outcomes from the participation of TNCs in the host country, in particular its bargaining leverage to ensure that the greatest possible share of rent from mining accrues to the host country.

3.2.1 Contribution of TNCs to capital and technology

This section assesses the theoretical argument that TNCs supplement the capital and technology of developing countries that would otherwise be lacking. The supplement assumption (that foreign resources supplement domestic resources, without which local production would be limited) and the resource generation assumption (that TNCs generate additional resources to utilise previously unused resources) justify the existence of TNCs in host countries, according to neo-classical theorists (Jenkins, 1987:19). In the conceptualisation of earlier neo-classical theorists, Direct Foreign Investment (DFI)[22] increases the capital stock of host countries by way of capital flows that it facilitates between nations, encouraged through differential rates of return.

More recent neo-classical proponents of the product cycle model (for example, Vernon, 1979) and of 'internalisation' (including Buckley & Casson, 1985) ascribe the transfer of technology to the host country, by TNCs, as even more important than the transfer of capital, which because of external market imperfections, such technology transfers would otherwise not take place in developing host countries (Jenkins, 1987:20; Helleiner, 1989:1451). The imperative to sell a product at a competitive price, or at a

[22] DFI is defined by the IMF as 'investment made to acquire a lasting interest in a foreign enterprise with the purpose of having an effective voice in its management.' It includes all flows (direct or through affiliates) from the investor, as well as reinvestment earnings, net borrowing and equity capital (IMF 1985, cited in Helleiner, 1989:1445).

lower cost, when the product cycle is at a mature and therefore standardised stage,[23] enables developing countries to obtain technology at relatively favourable terms, through TNCs, according to the model (Vernon, 1979, cited in Buckley, 1985:8).

Neo-fundamentalists share the neo-classical arguments that foreign capital complements rather than displaces indigenous capital through benefits such as technology and capital transfers; that TNCs supplement and generate additional resources; and that TNCs open the markets of developed countries for the developing countries (Warren,[24] 1980, cited in Jenkins, 1987:31 and 32). Emmanuel (1976) emphasised in particular the low-cost technological contributions of TNCs to host countries (cited in Jenkins, 1987:32). The market-seeking production activities of firms that the product cycle model emphasises nevertheless fail to explain resource-based, efficiency-seeking or strategic asset-acquiring DFI (Dunning, 1993:71).

However, according to the 'real options view of investment', an initial 'wait and see' attitude of investors may encourage investors to postpone their investments. The real options view is based on the assumption of irreversible investment costs (namely, the capital loss to the investor when disposing of investment goods in a second-hand market) and of the uncertainty of future pay-offs and of future output prices. The greater the uncertainty and the higher the value of the potential investment, the greater would be the likelihood that the firm would postpone its investment decision. Possible investments that foreign companies possess elsewhere would likely ease losses in returns that they might incur from the postponements (Dixit & Pindyck, 1994, cited in Andersson, 2000:79). The 'real options' approach is highly relevant in the African context (Andersson, 2000:79).

The real options approach is contrary to the neo-classical model of investment of Jorgenson (1963). Jorgenson's model asserts that the firm chooses its capital stock so as to maximise the present value of the future cash flow, assumed to be known with

[23] The cost is also reduced because the labour-intensive stage of production that marks the mature stage is carried out in less developed countries where labour is cheap.
[24] One of the main proponents of neo-fundamentalism.

certainty, and it also assumes that the firm can sell the excess capital without a loss. That is, the firm chooses its capital stock to equalise the marginal product of capital with the user cost of capital (cited in Andersson, 2000:79).

Moreover, in the analysis of neo-imperialists, practices that drain the surpluses or resources from especially Third World host countries, inter alia by way of repatriating monopoly profits, are considered to contribute to 'blocking the development[25] and socialist transformation'[26] and to the 'development of underdevelopment'[27] in host developing countries. Underdevelopment obstructs the capital accumulation that is essential for economic progress in host countries (Helleiner, 1989:1453; Jenkins, 1987:28, 29). The introduction of risks and the negative repercussions of locally disintegrated and externally dependent economies that TNCs' activities tend to generate, also promote underdevelopment, in the view of the dependency school (Helleiner, 1989:1454; Padayachee, 1995:164). The stagnation and decay of underdevelopment created by the participation of TNCs in developing countries would, in fact inhibit technical progress in the host country, according to Lenin (1917, cited in Jenkins, 1987:27, 28). These activities of TNCs contrast with the resource generation and supplement assumptions of neo-classical theorists that TNCs play a positive role in the development of host countries.

Also, financing DFI by borrowing from local banks would make national gains in the supply of capital and foreign exchange unlikely. Additionally, if the resources are not invested within the host country, then the borrowing would effectively amount to a capital outflow (Helleiner, 1989:1455). Benefits of TNCs to the host countries depend on how much capital and foreign exchange is supplied and whether they merely substitute domestic inputs (Helleiner, 1989:1455).

An over-reliance on TNCs may create distortions in the local social, political and economic environment that may deflect development of the host countries from a more

[25] Amin's term.
[26] According to the Monthly Review School (especially Baran, Sweezy, O'Connor and Magdoff).
[27] Frank's term.

desirable and balanced path, in the conceptualisation of dependency theorists. The distortions may include a highly unequal income distribution, a strengthening of domestic concentrations of economic and political power together with the stifling of national entrepreneurship, indigenous research and development (Helleiner, 1989:1454). Furthermore, in the analysis of neo-imperialists, crucial decisions on production and on accumulation of TNCs follow the global interests of the parent company, which do not always suit the interests of local capital (Jenkins, 1987:29).

3.2.2 Returns to the local economy from the activities of mining TNCs

Exhaustible resources require adequate capturing of rent by the government and the reinvestment of the capital allowance component in alternative forms of capital assets, to promote national development and to maximise long-term revenue to compensate for depletion or their limited income and employment potential (Blignaut & Hassan, 2002:89-101; Blignaut & Hassan, 2001, cited in Cawood *et al*., 2001:157). The alternative renewable forms of capital assets that revenue from non-renewable resources should be invested in include the creation of new wealth and forms of renewable capital, such as human, social and physical capital, which are central to achieving sustainable development beyond mining (Pedro, 2004:6). Accordingly, the main determinants of the returns to the local economy from the activities of TNCs in the copper mining sector in Zambia considered in the study are: (i) increases in government revenue, and the foreign currency earnings of Zambia; and (ii) the development of the local capacities, especially the suppliers and workers of the mines.

(i) <u>The roles of mining TNCs in increasing government revenue and foreign currency earnings</u>

An adequate fiscal take from mining is necessary to enable the government to meet requirements of capital generation for reinvestment in projects and in social capital (Macfarlane, cited in Cawood *et al*., 2001:220 and 221). Accordingly, the tax system of the mining sector provides a measure of the integration of this sector to the rest of the economy (Bova, 2009:2). A reduced ability of governments to tax mobile factors (partly as a result of tax competition) that lowers government revenue put pressure on government expenditures in productive sectors[28] that are vital for the economic development of countries (see, for example, Ebrill *et al.*, 1999; IMF, 2005a; Glendy, 2006, cited in Volkering, 2009:3).

Rather than improving the revenue and resources of the government through supplementing foreign exchange earnings and the local savings of Third World host countries, TNCs drain the resources of these countries, in the conceptualisation of neo-imperialists and Global Reach theorists. Transfer-pricing practices, through certain accounting procedures that are not always reflected in the tax returns of subsidiaries, would also facilitate the draining of surpluses and have negative redistributive implications for developing countries, according to Global Reach theorists. The problem of transfer-pricing relates to "the absence of market friction in transactions between controlled persons and the resulting need to verify prices in such transactions for income tax purposes and, if necessary, to adjust for that absence" (Rosenbloom, 2005, cited in Bhat, 2009:1).

(ii) Roles of mining TNCs in promoting local capacities

In the case of non-renewable resources, it is necessary to develop not only mineral clusters but also lateral or down-stream businesses that have the potential to create employment and generate value-added rents and wealth, according to Pedro (2004:6). However, other theorists downplay the benefits of developing backward and forward linkages to mining, mainly because the capital-intensive nature of modern mining operations renders them heavily reliant on foreign capital, with poor local production linkages (Lewis, 1982; Auty, 1993, cited in Cawood et al., 2001:220, 221). These theorists consider fiscal linkages the strongest linkage between the mining sector and the national economy, rather than backward and forward linkages.

Moreover, contrary to the claim of neo-classical and neo-fundamentalist theorists that TNCs supplement local resources, Global Reach theorists argue that certain practices of TNCs may contribute to the displacement or substitution of local capital and

[28] Such as infrastructure, education and healthcare.

entrepreneurship (Hirschman, 1969, cited in Jenkins, 1987:25). Such practices encompass restrictive business practices[29] through clauses that tie various inputs to the technology suppliers, restricting exports to divide world markets (through TNCs acting collectively as cartels, or through collusions) and the packaged nature of DFI, which includes the import of capital and management (Jenkins, 1987:24, 25). Neo-imperialists share the view that TNCs substitute local capacities. De-nationalisation (that is, increasing foreign control of the local economy), the displacing and acquiring of profitable local capital and the moving of TNCs into new activities, while relegating local capital to the least profitable and most competitive sectors, also play a subversive role in the host country, in the analysis of these theorists.

The practices of TNCs of substituting local capital reduce the local bourgeoisie to a 'comprador' or dependent bourgeoisie position, incapable of playing their historic role of promoting capitalist development, according to neo-imperialists (Jenkins, 1987:29). In contrast, the Latin American dependency theorists discourage a close relationship between the local bourgeoisie and foreign capitalists, which they argue would not provide a basis for national development (Padayachee, 1995:164). The 'dependency' argument is not shared by neo-fundamentalists, who maintain that TNCs reduce, rather than cause dependence of host countries, by fortifying and diversifying host countries' economies or by developing these countries' productive forces (Jenkins, 1987:31).

3.2.3 Roles of the government in promoting more beneficial outcomes from the participation of TNCs in the host country

The roles of the government in promoting more beneficial outcomes from the participation of TNCs in the host country are examined by assessing government measures necessary for attracting TNCs and to guide their activities to more advantageous outcomes for the host country. The bargaining role of the government in directing the activities of TNCs towards more successful results is also explored.

[29] To preserve monopoly rent.

3.2.3.1 Government measures to attract TNCs

The policy implications drawn from Rugman's neo-classical risk-aversion hypothesis are that governments of developing countries should promote greater stability to attract TNCs and provide a favourable climate to attract investments by TNCs. The hypothesis considers TNCs as efficient entities and views the location of a firm's investment as a function, in addition to the geographic distribution of its existing assets, also of the firm's perception of uncertainties in potential host countries. Liberal trade policies and unrestricted trade and industrial policies are considered important for attracting DFI. Policies to attract TNCs should, though, not promote distortions (Rugman, cited in Jenkins, 1987:22; Dunning, 1993:173).

However, the marginal increases in the share of DFI in developing countries in the 1990s, regardless of extensive liberalisation policies, somewhat discredit the argument that liberal policies would attract well sought-after global TNCs (Chang, 1998:236). As long as restrictive government policies are not too excessive but are stable, with predictable changes, they do not represent a major factor influencing the locational decisions of especially larger TNCs and those with higher sunk costs[30] that would likely accommodate these policies (Chang, 1998:237). The lowering of government taxes (or tax incentives, tax holidays and differentiated tax structures) proves less important than the general investment climate and policies affecting specific sectors in attracting DFI (Padayachee, 1995:166).

Moreover, DFI would stimulate rapid economic growth only once a certain economic development threshold is attained, according to a study by Blomstom, Lepzig and Zeyan (cited in Padayachee, 1995:165). Rather than causing rapid industrialisation, DFI therefore seems to take place as a consequence of rapid industrialisation. Accordingly, the development of local capacities (which includes a stronger regulatory framework) and resources to enhance the general economic position of the host country and a stable political climate seem more important than liberal policies in attracting less footloose global TNCs (Chang, 1998). Section 3.3.1.2 elaborates on some factors that increased

[30] A cost that has been incurred and cannot be reversed (Investopedia, 2010).

the capacity of the governments in developmental states, which would also enhance the bargaining leverage of the government to ensure more successful outcomes for the host country from the activities of TNCs.

3.2.3.2 Government measures to promote more advantageous outcomes for the host country

A further policy prescription attributable to both earlier neo-classical theorists and ‘internalisation theorists’ is that government regulation of TNCs’ activities, considered as always inefficient, needs to be removed or discouraged (Jenkins, 1987:22; Padayachee, 1995:164). However, liberal policies and the neo-classical appeal for the elimination of government interference in the economy may not necessarily have positive outcomes for the country. For instance, corporate objectives of TNCs to maximise profits over welfare might in fact have adverse consequences on the country and might sabotage trade and industrial policies of host countries’ governments (Panic, 1998:264). Moreover, evidence exists that in cases where the state has played an active role, the local economy has benefited greatly from internationalisation (Evans, 1998). In particular, developmental theorists consider strong state involvement as necessary to effectively impact on decisions of TNCs (Jenkins, 1987:25, 26).

Strong bargaining skills (elaborated upon in Section 3.2.3.3) and effective government measures are also necessary in the mining sector to ensure a greater capturing of the share of the benefits of the rent element for the host country from the activities of TNCs (Chang, 1998:238; UNECA, cited in Action Aid International, Christian Aid, Open Society Institute of Southern Africa, Third World Network Africa & Tax Justice Network Africa, 2009:x, 3). To reverse the ‘paradox of plenty’ and to obtain mineral wealth from mining revenue, necessary for development, the building of institutional capacities seems to be the most urgent challenge of minerals-dependent economies. Weak government institutions have been the root cause of Africa’s ‘resource curse’ (Action Aid International *et al*., 2009:viii, x; Bebbington, Hinojosa, Burneo & Warnaars, 2008:10). Good governance through effective institutions was fundamental in enabling Botswana with its rich natural resources to enjoy economic growth (Action

Aid International *et al*., 2009:3; Iimi, 2001:24).

Measures to maximise long-term mineral revenue, enabled through an adequate capturing of rent by the government and reinvestment of its capital allowance components in alternative forms of capital assets, and to buffer short-term distortions of mineral price volatility are also necessary to limit the 'resource curse' (Lewis, 1982 and Auty, 1993, cited in Cawood *et al*., 2001:220 and 221). Better institutional capacities, which are lacking in many African mining economies, specifically require a reform of the laws, policies and institutions that govern financial payments made by mining corporations. The distribution of revenue from mineral rent is rarely a simple technocratic process but rather the result of complex political forces, requiring government policies that will ensure acceptable distributional balance among recipients of mineral rents (Cawood *et al*., 2001:153; Crowson, 1998, cited in Shen, 2001:11).

The combined effect of taxation and spending represents an important avenue through which a more equitable distribution of income from mining becomes possible (Volkerink, 2009:3). However, the government has to balance its fiscal take from mining (to meet requirements of capital generation for reinvestment in projects and in social capital), with a firm's willingness to invest (Macfarlane, cited in Cawood *et al*., 2001:6; Otto, 2001:1). Too high taxes may prompt foreign investors to invest elsewhere. Conversely, if taxes are too low as is often the case with African countries competing for foreign mineral investment, the rent from mining dissipates almost exclusively to mining TNCs. These governments then needlessly forgo the collection of a fair share of mining rent (Action Aid International *et al*., 2009:vii, viii, x; Cawood *et al*., 2001:153; Otto, 2001:1).

Stabilisation funds, aimed at reducing the impact of commodity price volatility on the economy, which would in turn improve greater predictability of the budget by stabilising spending patterns, may also achieve greater fiscal stability and discipline (Pedro, 2004:12; Luong & Weinthal, 2006:40). Again, strong state institutions, emphasising oversight, transparency and an independent judiciary, are necessary for stabilisation funds to work, or else these funds could inadvertently reinforce the power and authoritarian tendencies in mineral-rich countries (Luong & Weinthal, 2006:40). Furthermore, studies suggest that in addition to better regulation, increased benefits can be achieved from DFI through greater transparency of foreign operations and by subjecting TNCs to competition from both local and other foreign firms (Padayachee, 1995:166).

Furthermore, the government should play a more proactive role in the selection process and in directing the activities of TNCs. In particular, rather than accepting footloose TNCs that are merely involved in cross-border linkages, the government should select DFI from global firms, which are likely to have significant positive spin-offs for the host countries. Global firms possess longer-term commitments and transfer skills and technology to the host country, which appears to have the strongest potential for indigenous development (Padayachee, 1995:173). Global firms are therefore important avenues for transferring expertise, finance and managerial assistance to local firms and for upgrading and consolidating technology and human resource capabilities of host countries (Gordon, 1994, cited in Padayachee, 1995:166).

Moreover, industrial policies should aim to attract especially global TNCs that reinforce competitive advantages and that promote partnerships with host countries' industrial and retail outlets, through vertical or backward and forward linkages, or through horizontal linkages. Such linkages would build local capacities, by improving human capital, manufacturing competitiveness and technological capabilities (Padayachee, 1995:173). Horizontal linkages, involving partnerships of local industries with global TNCs' research activities, will have positive local spillover or externality effects, including increased human capital development. These could potentially translate into dynamic comparative advantages for the host country (Padayachee, 1995:173). Especially vertical-linkages, where global TNCs outsource less core activities to producers of the host countries (to ensure that the capabilities of local suppliers match and integrate with the value chain of TNCs), promote employment opportunities, know-how and appropriate resources (including technology) to local suppliers (Kozul-Wright, 1998:150, 152, 154).

3.2.3.3 The role of bargaining of the government in affecting more successful outcomes from TNCs' activities

Host governments could influence the activities of TNCs in their countries, especially by way of bargaining, on account of the potential that exists for rent or quasi-rent, pertaining to oligopoly, and because of transfer-pricing practices and other market imperfections that characterise the activities of TNCs, according to Chang (1998:237). Employing the potentials of the country to attract and steer the activities of TNCs within targeted desired directions would also enable the government to enhance the economic welfare of their countries (Chang, 1998:237; Helleiner, 1989:1453, 1461). Neo-fundamentalists also consider the international competition among TNCs important for increasing the bargaining power of developing countries.

However, the assumptions of the bargaining paradigm that relationships among negotiating parties are established as a result of free choice and that the state acts in the interest of the members of its subjects do not always hold, especially in developing countries (Bruno Continni, 1968, cited in Lungu, 2008:3; Padayachee, 1995:164). The bargaining paradigm gives insufficient consideration to the potential for interest group divergences, which are influenced by political factors (especially captive powerful interests that determine the policy direction of the state) and by competition within the host country that may constrain bargaining. Forces outside the volition of the state may coerce the government to follow certain actions (Philips, 1976, cited in Helleiner, 1989:1462; Padayachee, 1995:164; Lungu, 2008:4).

Nonetheless, despite these limitations, certain approaches of the host government in the bargaining process would ensure more beneficial outcomes for the host country from the activities of TNCs and may be more important than a universal liberal policy.[31] Liberal policies would, in fact, reduce the manoeuvring power of the host country. A differentiated strategic approach that takes into account the contextual realities, the

[31] Encouraged by the IMF and the World Bank.

technological and other roles of the industry and the relative bargaining strengths of TNCs and governments to enable host countries to extract the maximum benefits possible from TNCs has proved more important than a universal liberal policy, according to Chang (1998:238).

New domestic industries require a more liberal policy, while tougher localisation requirements, as well as other restrictions on TNCs are more appropriate when the technological capabilities of the local industry are well developed (Chang, 1998:238). The bargaining success of the host country is further determined by the information, political will, alliances, or competitiveness of the country in relation to other countries (and firms) and by domestic organisation (Helleiner, 1989:1461). The location and quality of minerals prove especially important in attracting TNCs in the mineral sector (Helleiner, 1989:1461).

A corporatist role of the state that characterises developmental states, discussed in Section 3.3.1.2, denoting that the leadership role of the state is more important than its follower role, will also increase its bargaining leverage to deal more effectively with private foreign and internal economic interests. A corporatist role would enable the government to determine the role of TNCs' capital, set terms that attract foreign capital (without conflicting with TNCs) and to serve the domestic economic development of the state (Leftwich, 1995:417). A leadership role necessitates a bolstering of the state's capacity.

Accordingly, in contrast to developing countries, the power of developmental states was first consolidated before foreign capital interests expanded, which augmented the bargaining leverage of governments in these countries (Leftwich, 1995:418). On the other hand, a host country's bargaining leverage is particularly weak if, as is the case with mineral exploration activities, opportunities for profitable activities are doubtful (Helleiner, 1989:1463). Also, the bargaining strengths of host countries are weakest during periods before foreign firms have sunk inputs into the country, while the capacity of the TNCs to extract concessions from the host country will decline once it has sunk its own inputs into the project (Helleiner, 1989:1463).

3.3 A REVIEW OF PERSPECTIVES ON THE ROLES OF THE STATE

The roles of the state in the privatisation of SOEs and in influencing the activities of TNCs, assessed above, are subsets of the theoretical review of the roles of the state in the economy. The exposition of the roles of the state in the economy serves largely to put the pro-market, minimal government interventionist policies of the IMF and World Bank, instituted alongside the privatisation policies of the mines, into context. The discussion below examines first the theoretical perspectives on the roles of the government in the economy. This is followed by an examination of the theoretical arguments of the interests promoted through the state as well as by market-oriented policies.

3.3.1 The roles of the government in the economy

The various theoretical views on the roles of the government in the economy are evaluated below, followed by a brief consideration of measures considered necessary to enhance the capacity of the state in the economy. Main criteria that have accounted for the high capacity of developmental states that contributed to the exemplary growth and development of these countries are drawn upon in evaluating the capacity of the state.

3.3.1.1 Theoretical perspectives on the roles of the government in the economy

Besides recognition of a role for the government in promoting law and order and in establishing physical infrastructure, the neo-classical approach that favours pro-market or liberal polices demands a reduction in the role of the government in the economy or a de-politicisation of the economy. This approach permeates the SAPs[32] and stabilisation policies[33] of the IMF and the World Bank. Liberalisation involves the removal of government interference in financial and capital markets and the elimination of barriers to trade, enabling the free movement of goods, services, investment and capital flows between countries (Stiglitz, 2002:59).

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[32] Involve policies of getting the prices right, by eliminating subsidies and protection, raising interest rates, lowering wages, devaluing the currency and privatisation (Fine and Stoneman, 1996:9).
[33] Involve reduction of government and balance of payment deficits (Fine and Stoneman, 1996:9).

The neo-classical theorists' criticisms of the state are thus not confined to government policies of import substitution and of financial repression but are levelled at the necessity of the state itself, considered as an irrational, corrupting force that prevents the rational management of the economy (cited in Chang, 1994:1, 8). Constraints on public action that limit government policies and generate internal political realignment also became more binding alongside foreign debt obligations and policy pressures of IMF and World Bank conditionalities (Shapiro and Taylor, 1990:876). The recommendation to de-politicise the economy, through diminishing the roles of those that can exercise political influence, will, more than market liberalisation, remain the most long-lasting legacy of the neo-liberal counter-revolution (Chang, 1994:8).

Neo-classical theorists consider the 'invisible hand' of the competitive market as more effective than the government in reconciling the different desires of various individuals and the only viable path to development, which cannot be controlled by the state (cited in Chang, 1994:3). The premise that private agents have perfect foresight informed the neo-classical argument that the price mechanism, determined through markets, promotes robust growth and an effective allocation of resources. The price mechanism is also viewed as more capable than short- and long-term developmental goals of the government in achieving both short-term allocative efficiency and long-run dynamic efficiency (Williamson, 1990, cited in Stiglitz, 1998:1; Chang, 1994:3).

Various counter-arguments against a minimalist non-interventionist role for the state takes specifically market failure as the point of departure. The market failure approaches describe a strong role for the government in complementing markets,[34] in the context of imperfect information and incomplete markets, by way of correcting market failures, such as externalities and economies of scale and through the development of infant industries and public goods[35] and in the building of

[34] That, singly, would not always yield efficient outcomes and socially acceptable distributions (a function that the Washington consensus fails to take into account).
[35] Including maintaining law and order.

infrastructure[36] (Fine & Stoneman, 1996:15; Stiglitz, 1998:24-25). Other theorists draw further upon recent endogenous growth theories or 'new' growth theories that emphasise increasing returns or expansionary spillovers through investment in education (cited in Amsden, 1997:469, 470; Fine & Stoneman, 1996:15).

Stiglitz also envisages a crucial role for the government in the building of human capital and especially in the transfer of technology, both of which are key to development.[37] In the absence of building these, the gap in public investment in human capital and in the transfer of technology (which has returns greater than research and development, when countries are not operating at the technological frontier), would unlikely be filled by the market. The state also has an important role in promoting fundamentals, such as economic policies, environmental protection and in the regulation of social protection and welfare (Stiglitz, 1998:5, 6, 25, 26, 32).

Moreover, available evidence shows that the state-market dichotomy conceptualised by neo-classical theorists, as well as the notion of a balance between the state and the market, is misplaced in the African context. In fact, the provision of infrastructure, through state action, could extend the market. Evidence of public *crowding-in* for private and foreign investment is stronger than the contrary in these countries (Bangura & Gibbon, cited in Fine & Stoneman, 1996:19). The state nevertheless needs to withdraw once it completed its effective catalytic role, according to Stiglitz (1998:24, 25).

However, Amsden criticises the endogenous growth theory of expansionary spillovers through investment in education, arguing that in the absence of industrial policies to enable the absorption of school leavers, an unexpected brain drain and unemployment would preclude increasing returns through investment in education. Instead, Amsden shifts the focus to the need for establishing industrial policies (Amsden, 1997:469, 470). The market failure approach also omitted to take into account the capacity of the state to

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[36] Such as education, health and roads.
[37] Foreign Direct Investment (FDI) represents a policy through which the transfer of technology can be promoted (Stiglitz, 1998:26).

identify and to implement policies to correct for market failures (Fine & Stoneman, 1996:15).

3.3.1.2 Measures enhancing the capacity of the state in the economy

Instead of a wholesale reduction or a de-politicisation of the state, institutional change would lower the costs associated with state intervention. The political school, whose point of departure is the lack of political analysis of the 'market failure approach' and that seeks to identify the conditions under which the state is capable of being developmental, suggests an appropriate interventionist role for the government (Fine and Stoneman, 1996:15). A high capacity of the state, characteristic of developmental states, plays a fundamental role in promoting the hugely successful growth and development of the South East Asian 'tigers'.

A developmental state is defined as a state whose politics have concentrated sufficient power, autonomy and capacity at the centre to shape, pursue and encourage the achievements of explicit developmental objectives, either by establishing and promoting the conditions for economic growth by organising it directly or a varying combination of both (Leftwich, 1995:401). Developmental states tend to have well distributed benefits, with high growth rates, measured by a high Human Development Index (HDI)[38] (Leftwich, 1995:418). Three components characteristic of a developmental state that are relevant to the Zambian mining sector and which could aid analyses of the capacity of the Zambian state, include the promotion of economic bureaucracies that enjoy power and competence and are insulated; a corporatist role of the state over other economic interests; and effective industrial policies.[39]

(i) Economic bureaucracies that enjoy power and competence and are insulated

In the context of a world of limited mobility, a reform of the state and a better political management of the economy, together with institutional change, would be more suitable options for over-politicisation than the price mechanism through the market that neo-

[38] Measures national income, life expectancies and education.

[39] Other measures, not applicable to the study, considered necessary for a developmental state include the establishment of a developmental elite and an ability to control civic society.

classical theorists favour. These options would also be more effective than correct prices for achieving long-term developmental goals, in the view of Chang (1994:10-11). A long-term vision of the state that would improve the 'entrepreneurial vision' of the state was critical to the development of developmental states and of several developed countries. A long-term vision would best be achieved through effective institutions, which the government needs to build (Chang, 1994:13).

The economic bureaucracies of developmental states, managed by institutions that organise the interaction between the state and the economy, act as core centres for strategic economic direction and co-ordination. In contrast to the generality of planning institutions of many developing countries, these core economic bureaucracies, on account of their relative autonomy in economic affairs,[40] have real power, possess high technical competence and are insulated from shaping developmental policies (Leftwich, 1995:412, 414). For example, the Economic Planning Board (EPB) of South Korea that was crucial in contributing to the economic success of South Korea, had significant scope to manoeuvre (Kim & Leipziger, 1993:29, 30).

(ii) <u>A state that has a corporatist role</u>

The bargaining leverage of the state with TNCs and the debate of the minimalist or interventionist role of the state in its relation with TNCs, discussed respectively in Sections 3.2.3.3 and 3.3.1.1, are subsets of the question regarding the capacity of the state. A corporatist role of the government over other economic interests (including those of TNCs and of the IMF and the World Bank) would contribute to more effective economic development that would promote the capacity of the state to deal effectively with private foreign and internal economic interests (Leftwich, 1995:415). Developmental states possess an adequate corporatist role to enable them to determine the roles of TNCs' capital, set terms that attract foreign capital (without conflicting with the TNCs) and to serve the domestic economic development of the state (Leftwich, 1995:417). This argument coincides with Chang's view that the government should formulate its own 'choice sets' that would promote national interests, rather than

[40] Parliament does not have a great influence on the economy.

moving to a given optimal 'choice set' (Chang, 1994:13). Moreover, contrary to what is generally the case in developing countries, the corporatist role of the state also involves the consolidation of the power of developmental states before foreign capital interests are expanded (Leftwich, 1995:418).

(iii) Effective industrial policies

A consolidation of power that also increases the capacity of the state to attract TNCs could significantly be achieved through industrial policies that promote local capacities (Evans, 1998). In the absence of tariffs and quotas, competition from more established TNCs, enabled through unrestricted policies, would impede the development of national firms, while subsidies would promote the resources, expertise and efficiency of national firms closer to the level of TNCs (Panic, 1998:264). Accordingly, rather than getting prices 'right' determined through the market getting prices 'wrong' (for example, through tariffs, quotas and subsidies) created profitable investment opportunities that accounted significantly for South Korea's growth (Amsden, 1989:14).

Competent local capacities in South Korea were developed through the nurturing of local conglomerates and prompting them to become internationally competitive (Evans, 1998; Amsden, 1997:469-470). Trade barriers and subsidies have promoted local industries in developmental states but require a degree of good government discipline, that is, 'guarded capitalism' (Amsden, 1989:14; Chang, 1993:151). However, it is important to first assess the costs of distortions (especially product distortions) associated with trade protection (Rodrik, 1992).

3.3.2 Interests promoted through the state and market-oriented policies

A political economy approach is pertinent in assessing the manner in which the surpluses of the economic sectors are redistributed with a change in ownership. A political economy approach takes cognisance not only of pure economic issues but also of political aspects, involving an inquiry into the nature of power and political behaviour in the development process and the competition for authority. The economic aspect in a political economic framework encompasses an examination of the allocation and exchange of scarce resources, including political and social resources (Uphoff & Ilchman, 1972, cited in Low, 1991:4). The pivotal role of the state and the impact of economic, social, political (and even cultural) policies on the generation and redistribution of power are acknowledged in this approach (Low, 1991:4).

The state is considered as an organisation controlled by interest groups, politicians and bureaucrats that use the state for their own self-interests, with socially undesirable outcomes, according to neo-classical models (Chang, 1994:2). Chang challenges the degree to which the self-interest assumptions pervade the political socialisation process, in light of the greater institutional constraints on self-seeking that the state faces over the market. Moreover, politicians' consideration of themselves as guardians of public interests and other interests groups predispose them to serve public rather than personal objectives. In fact, some of the most successful economies in East Asia have emerged as a result of structural change, facilitated through high political participation (Chang, 1994:9).

Furthermore, class interests are not the prerogative of government ownership but are represented through both the state and the market (Fine & Stoneman, 1996:19). For instance, rather than being neutral, the pro-market forces and less government interventionist policies promoted by neo-classical proponents favour capital, while diminishing the influence of workers. Also, the idea of a 'leaner, fitter state', which effectively leaves economic decisions to the market, amounts to disguised intervention on behalf of capital (especially foreign capital), while government intervention on behalf of labour is withdrawn. Fine and Stoneman further maintain that privatisation represents not merely a withdrawal of the state in favour of the market but is a particular form of intervention, which, depending on its form in immediate implementation and subsequent regulation, favours some capitalists, whilst disadvantaging others.

Moreover, the roles of the IMF and the World Bank, whose policies are fashioned according to neo-classical views, have been to create, preserve and promote capitalist relations in production and exchange. This was achieved by pressurising especially smaller states, from the late 1980s and the 1990s, to liberalise and re-orient state intervention towards ‘creating an enabling environment for businesses. More recently, the roles of the World Bank and the IMF, which have shifted over the years, have largely been aimed toward ensuring the profitable functioning of a core of private capital, even if this requires concretionary policies. Such a practice contrasts with the more overtly interventionist Keynesian policies that were prevalent during the immediate post-colonial period. Concretionary policies undermine a more broadly based accumulation of capital (Fine & Stoneman, 1996:14, 23).

Bond and Manyanya extend this argument further, claiming that in addition to SAPs and the stabilisation policies of the IMF that favour certain elite classes over marginalised groups (such as indigenous business and workers), state ruling parties may also resist radical change in social relations. Radical change is considered necessary for true transformation. For instance, governments’ increasing acceptance of the World Bank and IMF policies, together with corrupt government practices that do not benefit the masses, signify a realignment of the government away from the more marginalised, including workers and peasants, towards alliances with those that would assist them to remain in power. Accordingly, these theorists argue that the imperialist hold of the IMF and the World Bank together with government policies have dramatically changed the social relations in favour of capital, especially foreign capital and the government elite, over the workers, who are disadvantaged by neo-liberal policies (Bond & Manyanya, 2002:62, 63, 71, 79).

Fine and Stoneman (1996) recognise the significant influence that the IMF and the World Bank possess in building class structures but question the inevitability of certain outcomes of the policies of these bodies suggested by Bond and Manyanya’s conceptualisation. These theorists consider the view of the IMF and the World Bank as instruments of foreign capital and conduits of well-defined capital interests that simply impose neo-colonial imperatives as overly deterministic. A simplistic class-based classification, such as a clear distinction between indigenous and TNCs’ capital and capital and non-capital producers, is further viewed as insufficient. It also fails to take into account the possibility that these classifications may vary over time and across and within countries and the heterogeneity within economic sectors that involve a portfolio of complex activities and interests (Fine & Stoneman, 1996:14).

CHAPTER 4

4. BACKGROUND OF THE ZAMBIAN MINING SECTOR

This chapter presents a brief overview of the Zambian economy to provide context to the mining sector. Main policies of the Kaunda and the Chiluba governments that influenced the mining sector are then examined. The examination also explores the impact of policies of the IMF and the World Bank that were intermittently introduced from 1983 and were more rigorously adopted in the 1990s under the Chiluba government. Furthermore, the redistribution of the resources of the mining sector and the consequences on Zambia's development and political economy under the different governments are considered. This is followed by an investigation of various economic indicators.

4.1 OVERVIEW OF THE ZAMBIAN ECONOMY

Substantial investments into the mining sector during the Federation years resulted in the Kaunda government inheriting at independence on 24 October 1964, a well-run, modern and technologically sophisticated mining sector infrastructure (MUZ, 1994:1). At independence, the copper mining sector contributed significantly to the Zambian economy. It accounted for 92% of total export earnings, 40% of GDP, 71% of government revenue and a third of employment in the direct productive sectors, amounting to about 50 000 workers (MUZ, 1994:1; Seidman, 1977:218). The high contribution of mining to the Zambian economy also reflects the poor economic status of the rest of the economy or the 'Dutch disease'[41] that the economy suffered at independence.

In the short term, the high copper prices alongside the policies of the Kaunda government of reallocating surpluses and taxes from mining to develop the rest of the economy, promoted a more rapid growth of the Zambian economy than was the case under Federal rule (World Bank, 1984, cited in Rakner, 2001:530). The growth was especially evident in copper production, the employment levels of the mining and other

[41] Refers to the deindustrialisation of an economy as a result of the discovery of a natural resource. The term was coined after this outcome occurred in Holland with the exploitation of North Sea Oil, which raised the value of the Dutch currency, rendering exports uncompetitive and causing its industry to decline (The Free Dictionary, 2010).

sectors, the manufacturing sectors and in the provision of social services (Cherv, 1989:126). Mining taxes were largely repatriated out of Zambia before independence under Federal rule (World Bank, 1984, cited in Rakner, 2001:530). The rapid growth of the Zambian economy, especially in the first decade of independence, shifted Zambia in 1969 to a middle-income country, with one of the highest GDPs in Africa (Seidman, 1977:218; World Bank, 1984, cited in Rakner, 2001:530; McGrath & Whiteside, 1989:169; The Economist Intelligence Unit, 2002:34; Fraser & Lungu, 2007:7).[42]

External factors, especially the collapse in the price of copper in 1974-75 after the first oil crisis in 1973 that culminated in the prolonged depression on the world market and considerably weakened Zambia's terms of trade, interrupted the rapid growth and negatively affected the rest of the Zambian economy (Cherv, 1989:126-127; Leistner, 1996:11.8; Rakner, 2001:530; Fraser & Lungu, 2007:8). The contribution of copper earnings to total government revenue dropped sharply, from 34% in 1974 to 13% in 1975, and remained at low levels for well over a decade (Burdette 1986:96, cited in Akwetey, 1994:53). In 1979, the second oil crisis and the resultant increases in interest rates alongside the slowing down of Zambia's development forced the Kaunda government to borrow to maintain the provision of social services and to finance industrialisation (Fraser & Lungu, 2007:8).

Despite the economic crises, the mining sector continued to be treated as a 'cash cow'[43] under Kaunda's government, 'milked' without corresponding investment in machinery and prospecting ventures. Moreover, as had been the case before 1969, the mines suffered from low investment in exploration and drilling. Consequently, no new mines were opened after 1979 (Fraser & Lungu, 2007:8). The production of copper also dropped dramatically, from a peak of 747 500 tons in 1969 and a high of 694 600 tons in 1976 to merely 257 000 tons in 2000, largely owing to increased production costs in the existing mines.

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[42] During this time, Zambia boasted a GDP higher than those of Brazil, Malaysia, Turkey and South Korea, three times that of Kenya and twice that of Egypt.

[43] Involving the redeployment of the resources of the mining sector to develop other sectors.

Accordingly, the drop in copper prices relative to the price of imports, alongside a continuation of the same consumption patterns created during the first decade after independence when the income from copper was high, greatly contributed towards the dramatic collapse of the Zambian economy between the 1970s and 1990s. Furthermore, the per capita income declined by 50% from 1974 to 1994, demoting Zambia to the 25th poorest country in the world in 1994 (Cherv, 1989:126; Leistner, 1996:11.8; Rakner, 2001:530, 531; Fraser & Lungu, 2007:8). In the context of foreign exchange shortages, the falling output of copper and trade deficits, Zambia became highly indebted from the 1980s (Leistner, 1996:11.8; Rakner, 2001:531). The country's high debt forced the Kaunda government to accept IMF and World Bank policies from 1983 that henceforth played an important role in directing economic development in Zambia.

4.2 POLICIES OF THE KAUNDA AND CHILUBA GOVERNMENTS AND OF THE IMF AND THE WORLD BANK

Several policy changes that the Kaunda and the Chiluba governments introduced in the mining sector influenced the development of the mining sector and the political economy of Zambia in distinct ways. As is noted above, external actors, in particular the IMF and the World Bank, also shaped the economic and mining sector policies of Zambia from the 1980s and their policies became more entrenched from the 1990s during Chiluba's government. The discussion below examines the mining policies of the Kaunda government and the policies of the IMF and the World Bank during Kaunda's government and their impact on the mining sector. This is followed by an overview of the policies of the Chiluba government, which were largely determined by the IMF and the World Bank, and their impact on the mining sector.

4.2.1 The mining policies of the Kaunda government

The policies that the Kaunda government adopted that constituted significant milestones in directing the development of the mining sector were, in chronological order: the Accommodation Period; the nationalisation of the mines; the granting of management control to TNCs; state control over the management of the mines; increases in government shareholding in mining companies; the merger of Nchanga Consolidated

Copper Mines (NCCM) and Roan Consolidated Copper Mines (RCM) to form the ZCCM and the NERP. These policies as well as those of the IMF and the World Bank that the Kaunda government adopted that also influenced mining policies in the 1980s are elaborated upon below.

Accommodation Period (1964-69)

During the Accommodation Period, the two foreign TNCs, Anglo American Corporation (AAC), operating in Zambia under Zambia Copper Investments Limited (ZCI) and the American Metal Climax (AMAX) that operated under the Roan Selection Trust (RST), were allowed to continue full ownership and control of the mines in Zambia. Moreover, the mining rights of these two private mining companies remained unaffected and continued to be held in perpetuity (Saasa, 1987:17, 26). However, despite the mining TNCs' uninterrupted ownership and control over the mines, some interventionist policies were introduced during the Accommodation Period by way of the far greater reallocation of surpluses from mining nationally than was the case in the pre-independence period.

A redirection of 13.5% of mineral royalties[44] to the new government that the Mining Ordinance (Amendment) Act of 1964 facilitated, and the reforms via the Muligesh Declaration limiting remittances of mining companies to only half of their profits,[45] enabled the higher redistribution of mining surpluses into Zambia. Prior to independence, the mineral royalties accrued to the British South African Company (BSA). Before limitations were placed on remittances, the mining TNCs tended to distribute over 80% of their profits as dividends, instead of reinvesting these in Zambia, which contributed to Zambian operations being grossly undercapitalised (Saasa, 1987:27).

The Kaunda government used the same tax formula for the mining companies that the BSA employed for many decades before independence, based on the LME prices and on gross taxable profits rather than on net profit. However, the private mining

[44] Based on the LME – prices, per ton per month less £8.
[45] While the other half had to be reinvested in Zambia.

companies objected to this formula of taxation under the Kaunda government.[46] The royalty and export tax of mining companies, as a percentage of gross taxable profits, totalled about 49.2%, comprising of 23% in royalties[47] and 26.2% in export tax (Turok, 1989:26; Sardanis, 2003:230, 231). Income tax amounted to 37.5%, which, together with the royalty and export tax (based on a tax on production, rather than on profit) enabled the Zambian government to receive taxes worth about 73% of profits from mining companies. This was high by international standards. The high taxes had an adverse impact especially on smaller, less profitable mining companies (Saasa, 1987:26, 37).

Dissatisfaction with the linking of the royalty formula to the LME prices of copper[48] and the tax on production rather than on profit, which private mining TNCs felt discouraged the development of high-cost low-grade mining, precipitated their demands for the replacement of the royalties and the export tax with a mineral tax. The mineral tax was to be based on net profit, rather than on LME prices (Sardanis, 2003:230; Saasa, 1987:28). The motivation for rejecting exactly the same tax formula that they had accepted before independence was also rooted in the fact that AAC, as the major shareholder in the BSA and through the share of royalties that it received from the RST,[49] had regained these taxes. This left the company largely unaffected by the amount it paid in royalties. During the Accommodation Period these taxes accrued to the Kaunda government (Sardanis, 2003:230).

<u>The nationalisation of the mines, instituted through the Matero Declaration (1969)</u>

The government decided to nationalise the mines shortly after its acquisition of majority shares in the manufacturing and importing sectors of the economy (Seidman, 1977:229). The Mulungushi reforms of 19 April 1968 initiated the process of nationalising the mines. The president declared in the Mulungushi reforms that all rights of ownership or partial ownership of minerals that had hitherto remained in the hands of the two private

46 Interview with Andrew Sardanis, 19 October 2003.
47 Or a rate per ton equal to 13.5% of the average LME quotation during the month less £8.
48 Which were erratic.
49 Interview with Andrew Sardanis, 19 October 2003.

mining companies, AAC and AMAX, as well as their exclusive prospecting and mining licenses, must revert to the state.

The nationalisation, instituted through the Matero Declaration of 11 August 1969, required an amendment of the constitution through a referendum and conferred government majority ownership over the mines (Fraser & Lungu, 2007:7; Maambo, 1998:4; Lungu & Silengo, 1997:13). The Mines Acquisition Act[50] established the new order in the ownership structure of the mines. The Act conferred all rights of ownership of minerals to the state, granting the state the power to acquire a 51% share in any new mine and obliging the owners of the existing mines, the ZCI and RST, to offer the government 51% of their shares,[51] in the form of 'A' class shares held by the newly-created Zambia Industrial and Mining Corporation (ZIMCO) (Lungu & Silengo, 1997:9; Fraser & Lungu, 2007:7; Maambo, 1998:4).

The change led to the creation of a new corporate structure that lasted for 12 years until 1982, when the two nationalised companies combined to form the ZCCM (Fraser & Lungu, 2007:7). The ZCI Holdings and RST became the minority shareholders, possessing 49% of 'B' class shares in these companies[52] and were respectively renamed NCCM and RCM (Maambo, 1998:4). After 1982 the ZCCM conglomerate operated until the mines were privatised between 1997 and 2000 (Fraser & Lungu, 2007:7).

The establishment of the 100% state-owned Mining Development Corporation (MINDECO) tasked with overseeing these bodies, together with the majority ownership that the government gained in the mining sector, granted the state greater influence over the copper mining industry (Saasa, 1987:38). The structure that the mining industry adopted from 1970 to 1982 is illustrated in Figure 4.1. However, during this time the government further relaxed the exchange controls in terms of dividends paid to non-Zambians. Private mining TNCs also continued to retain management control and other rights in the mining sector. This aspect is elaborated upon below.

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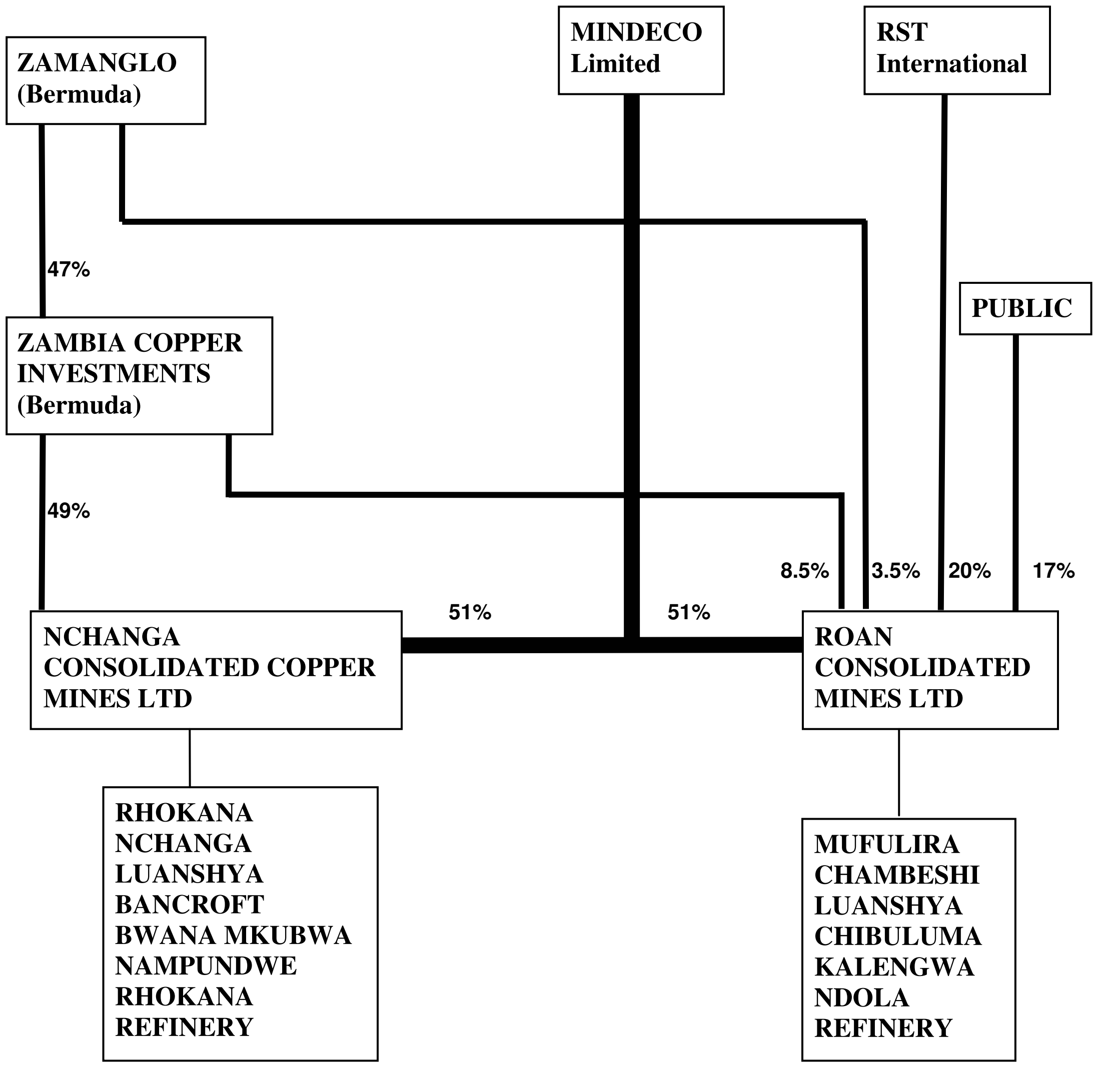
[50] The most significant feature of the Matero Declaration.
[51] Interviews with John Lungu, 10 October 2003 and M. Shandavu, 10 October 2003.
[52] Interview with Andrew Sardanis, 19 October 2003.

Figure 4.1: Structure of the mining industry between 1970 and 1982, after state majority ownership was introduced



Source: MINDECO (cited in Saacha, 1987:39).

The nationalisation policies introduced in Zambia between 1968 and 1972, rather than primarily because of a socialist predilection of the Kaunda government, were developed as a nationalistic and pragmatic response to the behaviour of private capital. The nationalisation policies involved the control and expansion of the parastatal sector over strategic parts of the economy, including the mining sector (Turok, 1989:47). After independence, the mining TNCs profited enormously, chiefly through excessive expatriation of profits gained during the boom that resulted in gross undercapitalisation, excessive local borrowing and a massive increase in foreign exchange expenditure on invisibles and on transfer pricing[53] that were lost to the government (Lungu & Silengo, 1997:13; MUZ, 1994:3; Turok, 1989:42).

The lack of new post-independence development in the mining sector by the private mining TNCs[54] and the accrual of substantial mining rents to the foreign mining companies were important motivations behind the nationalisation of the mines in Zambia. However, the nationalisation of the mines should not be confused with nationalisation in the sense of a government takeover of 100% ownership without compensation. On the contrary, under the agreement the government acquired the 51% controlling shares of the mines in exchange for fairly generous compensation to the former owners, AAC and AMAX (Seidman, 1977:229).

The compensation to the former mine owners that the government guaranteed for its acquisition of the 51% mining shares was in the form of ZIMCO bonds, at 6% interest and according to the book value of the mines. The payments were to be executed in semi-annual instalments over eight years to RST, at approximately K13.5 million per annum and to AAC at about K14.5 million per annum for 12 years, or an annual amount of about US$40 million to the mining companies, including interest to their parent companies, until 1978 (Seidman, 1977:229; Kaunda, 2002:18; Sardanis, 2003:238). The government was also to pay the companies a further US$21 million until 1982 (Seidman, 1977:229). Special provisions in the agreements enabled an acceleration of these payments, whereby the government had to pay two-thirds of the dividends received from each group if the sum exceeded the fixed annual payments during periods of high copper prices (Sardanis, 2003:238). The total compensation that the government paid to the mining companies in the form of bonds for nationalising the Zambian mines amounted to US$262 million (Seidman, 1977:235).

Since no statutory provisions existed to give the government explicit control over non-statutory industries, outright nationalisation, which generally involves some legislative

53 Whereby foreign investors manipulated production and revenue figures.
54 That these companies tended to blame on the royalty system.

statute or government decree, was not legally possible in Zambia during Kaunda's rule.[55] Rather than an outright nationalisation through an Act of Parliament, the Kaunda government elected to nationalise[56] or to gain controlling interests in the mines in a more tentative way, through 'derived control' of companies by means of the Articles of Association of the relevant companies and through a referendum. The choice of these methods was calculated not to cause concern among foreign investors (Turok, 1989:46; Lungu & Silengo, 1997:13).

Moreover, the government allowed TNCs to retain a substantial foreign minority interest in the parastatal companies. The parastatal companies were allowed a separate existence,[57] enabling them to operate largely as conventional businesses, rather than government departments. These concessions further support the argument that the government took care to avoid alienating foreign interests in Zambia (Turok, 1989:47).

To make the change in ownership rights more palatable, the Kaunda government granted the mining companies more favourable exchange controls and tax structures. The tax structures entailed more lenient post-nationalisation tax formulae for royalties and exports, through the Mineral Tax Act of 1970 that stemmed from the Matero Declaration (Seidman, 1977:232). These measures encompassed the new mineral tax formula, which replaced the royalties and the export tax (that, together with income taxes, were based on LME prices and on gross taxable profit[58]).

The new formula was calculated on profits after deduction of capital expenditures on mining operations, enabling the mining companies to pay only 51% of their *net profits* in the form of the new tax. In addition, the exchange control regulations permitting mining companies to remit only 50% of their profits were eliminated. However, income tax still had to be paid on the balance of the profits and a kind of PAYE formula was also introduced for the collection of the mineral tax, to circumvent delays in revenue

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[55] Even when the government possessed 100% shares in large companies the parastals had a legitimate and apparent permanent existence.
[56] After clause 18 of the Constitution of Zambia was repealed.
[57] That were not incorporated into the government departments.
[58] That dominated the mining sector before Independence under private ownership of the mines and, for a short period, after Independence, before the mines were nationalised.

collection until audited accounts of the mining companies became available (Sardanis, 2003:232, 238).

To encourage further mining development, the taxation of the mining industry, comprising of a combination of the mineral tax and the existing income tax, was limited to a maximum of 73%. Several allowances also lessened somewhat the tax burden on more profitable mining companies (Sardanis, 2003:238; Seidman, 1977:232; Saasa, 1987:37). Furthermore, new mines that achieved an average income of less than 12% of their average equity were provided with considerable tax refunds for up to three years. The new tax structures also encouraged investment specifically by way of not 'punishing' low-grade ore and high-cost mining ventures and were favourable to marginal mines (Seidman, 1977:232; Saasa, 1987:37). After their initial resistance, the mining TNCs eventually accepted nationalisation, which was also based on a realisation that the 51% majority ownership of the government could be advantageous, since the state would be sharing 51% of the costs and that state involvement would ensure industrial harmony.[59]

Granting private TNCs management controlling power (1970-1973)

After the nationalisation of the mines, the effective management or controlling power remained firmly vested during 1970-73 with the two foreign minority shareholders, the AAC and the RST. The benefits that AAC and RST enjoyed (elaborated upon in Table A1, in Annexure) were principally through their considerable power of veto and through their sole and exclusive right to provide certain services at a high fee. The services encompassed the sales and marketing of minerals and metals (at a fee of 1.5% of the gross turnover, plus 2% of the profits), financial, commercial, technical and other services (at a consultancy fee of 0.75% of turnover and 2% of profit, after mineral tax but before income tax) and recruitment services (Saasa 1987:40; Sardanis, 2003:269). Furthermore, the mining TNCs enjoyed preferential treatment in exchange control regulations, permitting the automatic externalisation of non-taxable profits, dividends, management fees and income from the sales of the private mining companies.

[59] Interview with Danny Kalyalya, 31 October 2003.

Additionally, the AAC and RST were protected against increases in several taxes, as long as their bonds were outstanding, and were allowed to write off all their expenditure in full in the year in which they were incurred. The mining TNCs were also paid a fixed minimum amount of ZIMCO bonds each year, irrespective of the profitability of the mines, and that had to be accelerated when profits were high. Moreover, the mining TNCs were protected against, among others, the government's defaulting on its ZIMCO bonds and against cancelling their management and sales or marketing contracts. Accordingly, although they were the minority shareholders, AAC and RST gained considerable control, particularly through their management, consulting and marketing privileges in the mining industry. This enabled them to accumulate significant sums at the time (Saasa, 1987:40).

However, rather than employing internal profits for investment – the Kaunda government's intention behind the more favourable tax reforms during 1970-73 – the mining TNCs preferred to borrow from external sources for expansion programmes. A large proportion of the TNCs' profits were allocated to dividends, instead of for reinvestment into the mining sector (Sardanis, 2003:268, 269; Saasa, 1987:40). Much of the savings and salaries of the expatriate community also left the country. The resources of Zambia were further externalised through the mining TNCs' depositing abroad the huge compensation that they received for nationalising the mines during Kaunda's government (Makgetla, 1994:119).

The enormous reduction in government taxes under the TNCs' management and government ownership was also significantly as a result of higher costs of mining TNCs, in addition to the fall in copper prices, tax reforms and the compensation the government had to pay the mining TNCs for nationalising the mines. The transfer-pricing practices[60] of mining TNCs, enabling the externalisation of considerable mining

[60] The mining companies also over-invoiced their costs, partly by adding their high management fees (averaging about US$6-7 million per year, paid directly to the mining TNCs) as an operating cost that contributed to the sharp increase in the costs of mining companies to about 20% from 1971-72 and possibly by over-invoicing imports from their own suppliers to reduce their share of taxable profit. The reported increases in the costs of the mines managed by AAC, by almost as much as that of AMAX

profit out of Zambia, and high management costs greatly contributed to the elevated costs of the mining TNCs under private management of the mines from 1970-73 (elaborated upon in Section 5.4.1.3 of Chapter 5). Government taxes fell from US$673 million in 1970 to US$65 million in 1972 (discussed in Section 4.4.20 below). The government was nevertheless still able to make decisions on the reallocation of a large share of the returns from mining for the development of other sectors of the economy.

Accordingly, the increasing dominance of the state sector during Kaunda's government was seemingly also a pragmatic response to the exploitation of Zambia's resources by private foreign capital. Ex-president Kaunda cites the transfer of profits out of Zambia rather than investing them in the Zambian mines, as an important reason for transferring the management control of the mines to the state (Turok, 1989:47).

Management control by the state (1973) and the introduction of Zambianisation policies

The Kaunda government revoked the management contracts of private TNCs in 1973. Subsequently, Zambian managers were appointed for the first time to take over management control of the mines (Sardanis, 2003:269). The decision to revoke the management contracts of TNCs was firstly motivated by the private managers' failure to reinvest a fair sum of their mining profits (much of which were transferred out of the country) in development projects in Zambia.[61] Secondly, it was motivated by tendencies of mining TNCs to employ external loans, instead of their share of profits, for investment into mining operations in Zambia. These practices, in addition to the total 'investment income' outflow and compensation payments, burdened Zambia's balance of payments (Seidman, 1977:233, 234).[62]

A third rationale was the decision to speed up Zambianisation policies in the mining industry,[63] through the Mulungushi Reforms, involving the deliberate placing of

despite being unaffected by the Mufulira disaster that augmented the cost of production of AMAX, serve as further evidence that AAC had probably over-invoiced their costs (Seidman, 1977:224, 233).

61 Also through transfer pricing practices, which reduced the annual government revenue, considerably.

62 As borrowed investment funds as well as the 7% to 9% interest had to be repaid.

63 Interview with Kenneth Kaunda, 11 October 2003.

educated and skilled Zambian technocrats into key management positions (Saasa, 1987:40). Under private ownership and management of the mines no Zambians had occupied managerial positions[64] before 1973. At the time, managers of the mining TNCs envisaged employing Zambians in general management positions only after 16 years.[65] A lack of the necessary managerial skills and experience for running big corporate companies (Zambia had only about a hundred graduates at independence) was another reason why Zambians generally occupied the lowest employment levels in the mining sector before 1973.[66]

The Kaunda government paid additional compensation to AAC and AMAX for the consequent loss of income arising from the premature termination of their management contracts and of the marketing contracts of their parent companies.[67] The payments, although not obligatory,[68] were ostensibly to pave the way for the appointment of Zambian managers. The government also redeemed all outstanding ZIMCO bonds to these companies in 1973 (Kaunda, 2002:19, 21; Saasa 1987:40). The amount paid for the premature termination of their management and services contracts amounted to K33 million (22 million pounds sterling) to AAC and K22 million (14.2 million pounds sterling) to AMAX, or a total of US$90 million over a three-year period (Seidman, 1977:235; Saasa 1987:40). The government was forced to take out a UK loan of US$150 million from the Euro-dollar market, at a floating rate of about 13%-15% interest,[69] to enable these payments (Seidman, 1977:235).

The timing of revoking the management power of the TNCs and the almost overnight redemption of the ZIMCO bonds to these companies to make way for the initial appointment of two black managing directors[70] proved disadvantageous to the development of the mines in the short term, according to Sardanis (2003:269). Because

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[64] Zambians were placed mostly in administrative and in personnel related positions and were excluded from occupying positions in critical areas, such as in cost accounting (interview with Danny Kalyalya, 31 October 2003).
[65] Interview with Kenneth Kaunda, 11 October 2003.
[66] Interviews with L. M. Lishomwa, 29 October 2003; Alick Lungu, 14 October 2003 and Danny Kalyalya, 31 October 2003.
[67] Interview with Andrew Sardanis, 19 October 2003.
[68] A lack of skilled Zambian manpower and the need to maintain overseas markets, with whom the private mining TNCs had contact, however, also influenced the government's decision to pay the private mining companies compensation for the termination of their management and marketing contracts (Seidman, 1977:229).
[69] Then encouraged by high copper prices which, shortly thereafter, remained depressed for almost a decade.
[70] The interviewee was one of the two Managing Directors (interview with Dave Phiri, 23 October 2003).

of the shortage of suitably qualified Zambians in the mining sector at the time, the government was obliged to re-hire most of the former expatriate managers to the positions that they had previously occupied, and this despite the fact that AAC and the RST had already received compensation for revoking their management contracts (Seidman, 1977:235-236). The redemption of the ZIMCO bonds also caused an added balance of payment and tax burden of about US$22 million a year (Kaunda, 2002:19; Seidman, 1977:235). Addressing the loopholes in the management contracts of the private mining companies might have been a better option for the Zambian economy than the government's revoking of the management contracts of the private sector.

Subsequent to paying AAC and AMAX for the premature termination of their management and marketing contracts, the NCCM and RCM became self-managing companies, with the choice of management resting directly with the government. Towards the end of 1973, following the cancellation of the marketing contracts with AAC and AMAX, the new Metal Marketing Corporation (MEMACO), a fully state-owned company, took over the responsibility for marketing Zambia's copper contracts. Despite its relative independence, the copper industry remained dependent on the TNCs for the provision of technical personnel, operational plans, research and development and for computer and management services (Saasa, 1987:40-41).

Although Zambian employees in the mining sector initially lacked experience, which caused some inefficiencies at the start of the Zambianisation process, in the medium term they soon gained the necessary experience to operate the mining sector competently. This was achieved mainly through extensive training and scholarship programmes for tertiary studies,[71] to selected pupils in the Copperbelt who were still at high school,[72] and through staff development programmes.[73] Zambianisation was further promoted by relieving or demoting expatriates from their positions.[74] The Zambianisation policies enabled Zambian managers to participate very competently in nearly all aspects of mining, especially at the operational and the technical levels and in

[71] Also at foreign Universities in Britain and the USA.
[72] Based on aptitude tests and Cambridge results (interview with John Lungu, 12 November 2003).
[73] Interviews with John Lungu, 12 November 2003; Andrew Sardanis, 19 October 2003; Dennis Wood, 21 October 2003; Wilphred Katoto, 12 November 2003; M. Shandavu, 10 October 2003 and Francis Kaunda, 20 October 2003.
[74] Interview with Alick Lungu, 14 October 2003.

the support services to the mining industry, until the mines were privatised (Kaunda, 2002:25; Seidman, 1977:227).[75]

The swift participation of a greater number of indigenous Zambians in the economy quickly promoted the emergence of a high-income Zambian elite.[76, 77] Also, the largely merit-based selection of highly skilled and competent Zambian managers that replaced the expatriates after the expiry of their contracts at the copper mines, contributed to the Zambianisation process in the medium term not being disruptive to the operations of the mining sector.[78] The education of Zambians and other benefits gained from the Zambianisation policies, together with reforms towards economic nationalisation, represent commendable successes of the Kaunda administration.[79] The training programmes to promote Zambianisation in the mining sector, which continued under the Chiluba government, ceased under private ownership of the mines.[80]

Government increases its shareholding in NCCM and RCM (1978-79) and the merger of RCM and NCCM to form the ZCCM (1982)

From 1978 to 1979, the government increased its shares in NCCM to 60.026% and in RCM to 60.62%, as compensation for loans that these two companies owed to the government. This was followed in 1982 by the merger (intended to rationalise the mining sector) of NCCM and RCM[81] that formed the ZCCM, a conglomerate of all the copper mining operations, which became the second largest copper mine in the world (Saasa, 1987:43; Maambo, 1998:Fig. 7). The main shareholder of the ZCCM was the government,[82] possessing 60.3% of the shares. The minority private shareholders consisted of ZCI, the South African subsidiary of AAC, with 27.3% of the shares. The remaining 12.4% of the shares were owned by other international investors, including

[75] Interviews with Zion Simwanza, December 2003; Gilbert Temba, 13 October 2003; John Lungu, 12 November 2003; Andrew Sardanis, 19 October 2003, Simon Capper, 30 October 2003; Fortune Kamusaki, 25 November 2003 and David Chilipamushi, 20 October 2003.

[76] Some obtained top political and civil service posts with high salaries and fringe benefits (Seidman, 1977:227).

[77] Interviews with Jack Jones, 22 October 2003; Alick Lungu, 14 October 2003; Dave Phiri, 23 October 2003; Andrew Sardanis, 19 October 2003; Dennis Wood, 21 October 2003; John Lungu, 12 November 2003; M. Shandavu, 10 October 2003; Francis Kaunda, 20 October 2003; David Chilipamushi, 20 October 2003; Charles Muchimba, 18 November 2003; Willie Sweta, 30 October 2003; Fortune Kamusaki, 25 November 2003 and Gilbert Temba, 13 October 2003.

[78] Interviews with Francis Kaunda, 20 October 2003; Danny Kalyalya, 31 October 2003; Willie Sweta, 30 October 2003; Fortune Kamusaki, 25 November 2003; M. Shandavu, 10 October 2003; Charles Muchimba, 18 November 2003; Simon Capper and Sipho Phiri, 30 October 2003; Gilbert Temba, 13 October 2003 and Emmanuel Mutati, 18 November 2003.

[79] Interview with Andrew Sardanis, 19 October 2003.

[80] Interview with M. Shandavu, 10 October 2003.

[81] Interview with M. Shandavu, 10 October 2003.

[82] Including the Ministry of Mines.

the RST (ZPA, 2000b:15; Transparency International, 2002:18).[83] Seven A-directors represented the government and five B-directors represented AAC on the board of the ZCCM.

Although the ZCCM failed to declare dividends, AAC remained a minority shareholder and a board member of the ZCCM until its privatisation. Its continued stay was partly because of the business opportunities such an arrangement held for its other businesses, mainly those strongly linked to the ZCCM as backward-linked industries.[84] However, by 2002 Anglo had an exit policy in Zambia, reflected also in the sales of its subsidiaries in Zambia and of its shares in the Shell company in Zambia.[85]

New Economic Reform Programme (NERP – 1987-88)

The SAPs of the IMF and policies of the World Bank that the Kaunda government adopted for most of the 1980s and since the 1990s were punctuated by the NERP[86] that the Kaunda government instituted from July 1987 to December 1988. The main theme of the NERP was 'growth from own resources'. Chiefly, the policies of the NERP entailed the re-institution of greater controls in the Zambian economy, on a similar basis to those that were in place pre-1982, before the introduction of the IMF and World Bank policies (McGrath and Whiteside, 1989:179; Cherv, 1989:138; Simutanyi, 1996:827). The NERP also differed in content from the IMF-supported programmes in the area of subsidies. The NERP reinstated the subsidies that the IMF policies withdrew. This was done because of their acute political significance, since their removal resulted in widespread popular unrest (Hanson & Hentz, 1999:486; McGrath & Whiteside, 1989:172).

Table A2 (in Annexure) elaborates on the controls that the Kaunda government instituted under the NERP. The main controls influencing the mining sector under the

[83] Interviews with Francis Kaunda, 20 October 2003; Silane Mwenechanya, 24 October 2003; Dave Phiri, 23 October 2003 and Andrew Sardanis, 19 October 2003.
[84] Interview with Silane Mwenechanya, 24 October 2003.
[85] Interview with Silane Mwenechanya, 24 October 2003.
[86] As an Interim National Development Plan (INDP).

NERP encompassed the fixing of the interest rate at a lower rate[87] and the suspension of the auctioning of the foreign exchange, through imposing greater controls over the foreign exchange market and by fixing the exchange rate of the kwacha.[88] Additionally, the government placed a ceiling on the country's debt service payment[89] and suspended additional interest payments owed to the IMF and the World Bank. The government also reintroduced direct price controls through the Price and Incomes Commission (Cherv, 1989:138, 139; Akwetey, 1994:56; Lungu & Silengo, 1997:15; Simutanyi, 1996:827; Hanson & Hentz, 1999:484; McGrath & Whiteside, 1989:172, 178).

However, the government was forced to abandon the NERP in 1989, within only eighteen months of its adoption, mainly owing to the impact of the collective Western financial embargo that foreign donors instituted in September 1987[90] as punishment for reverting to greater government controls in the economy. The financial embargo starved the country of aid assistance.[91] The spiralling economic crisis in 1988 and soaring debts brought the country's projects to a standstill. Apart from casting doubt on the creditworthiness of Zambia, the collective financial embargo also undermined the chance of the NERP proving itself as a viable alternative to SAPs in Zambia (Fraser & Lungu, 2007:9; Loxley, 1990:10 & Bates & Collier, 1993:428, cited in Akwetey, 1994:56; Simutanyi, 1996:827; Hanson & Hentz, 1999:484, 485; Cherv, 1989:134, 135, 138; The Economist Intelligence Unit, 1987a, cited in McGrath & Whiteside, 1989:180).

Subsequently, the donors made future support conditional on compliance with donor priorities. Compliance to donor conditions was also a prerequisite for drawing on the

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[87] Partly to assist indigenous firms that had been priced out of the market by the high interest rate policy of the IMF (Cherv, 1989:139).

[88] Through allocated foreign exchange control measures, via the Foreign Exchange Management Committee.

[89] At 10% of net foreign exchange earnings but only after essential import requirements were met (estimated to cover only one sixth of the unrescheduled debts (McGrath and Whiteside, 1989:172, 179; Cherv, 1989:133, 138; Akwetey, 1994:56; Simutanyi, 1996:827; Hanson & Hentz, 1999:484).

[90] Including the USA's Export-Import Bank and even Scandinavian donors, due to cross-conditionalities that the multilateral banks and donors imposed on Zambia.

[91] East European, Chinese and Scandinavian aid agencies complained of the difficult working environment, given the cool political relations and the breakdown of complementary aid supported programmes, previously supported by other bilaterals and multilaterals (Hanson & Hentz, 1999:485). Access to the second tranche of the Standby facility granted to Zambia in March 1986, of SDR 230 million from the IMF and SDR 69 million from the Compensatory Financing Facility (CFF) was blocked.

Extended Structural Adjustment Facility (ESAF).[92] In June 1989, the Kaunda government was forced to renegotiate with the World Bank and the IMF for a shadow programme that entailed a fully-fledged SAP (discussed below) (Simutanyi, 1996:827; Cherv, 1989:138; Fraser & Lungu, 2007:9).

The impact of the policies of the IMF and the World Bank on the development of the mining sector during Kaunda's government

Mining policies in Zambia were significantly influenced by the policies of the IMF and the World Bank from 1983, when Zambia embarked on its first systematic SAPs. From 1983 to 1991, the policies of the Kaunda government oscillated between accepting and abandoning the policies of the IMF and the World Bank. The government tended to adopt only some of the prescribed measures, influenced largely by electoral-maximising motives.[93] However, the suspension, delays and reduction of funds from the multilateral financial institutions[94] that prompted the Kaunda government to adopt the NERP from mid-1987 to 1988 in the context of the country's escalating debt problem,[95] also sabotaged the government's adherence to the SAPs (McGrath & Whiteside, 1989:179; World Bank, 1996:3; Lungu & Silengo, 1997:14, 15; The Economist Intelligence Unit, 2002:5). The policies of the IMF and the World Bank that the Kaunda government adopted before and after the NERP are considered below.

(i) Policies of the IMF and the World Bank before the NERP

The massive debts of the country and the inability to fund government revenue from mining income forced the Kaunda government to accept its first conditional loan from the IMF in 1973/4 and to enter its first World Bank SAPs in 1983. The adoption of SAPs enabled the International Financial Institutions (IFIs) to push the Zambian government into adopting economic liberalisation policies (Fraser & Lungu, 2007:9). Table A3 (in Annexure) lists the various measures that the IMF and the World Bank

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[92] The broader targets established in the Policy Framework Paper (PFP) and Rights Accumulation Programme (RAP) agreements contrasted with the strict quarterly targets characteristic of the three standby agreements that Zambia signed in the 1980s (Hanson & Hentz, 1999:487).

[93] Such as, to counter widespread riots on the Copperbelt, following the removal of food subsidies in 1986 and in 1991, which resulted in hikes in food prices.

[94] That also contributed to the failure of Zambia's auction system, introduced in 1985.

[95] In 1986 arrears to the IMF alone were around $100 million, which blocked the way to a new Standby agreement (Cherv, 1989:132).

imposed on the Zambian economy during Kaunda's government, which broadly include various liberalisation, de-regulation, rehabilitation and rationalisation policies. However, the policies of the multilateral institutions and other aid donors, aimed at rehabilitating the state enterprise (or parastatal) sector in the 1980s, generally proved to be of limited success, also in the mining sector (Craig, 2002:2). In particular, the demand management measures and supply measures of the SAPs had a negative impact on the workers and on the development of the mining sector, which continued during Chiluba's government.

Demand-side measures that involved cuts in the government deficit (about 20% in 1982), though seemed necessary, as continued high government expenditure was not sustainable in the context of the poor performance of the Zambian economy. Demand-side measures in the mining sector included the closure of three mines, reductions in employment and a decline in investment in the productive sectors of the economy, through the virtual halt in new investments in public projects. Although government expenditure cuts were necessary to reduce the high government deficit, lower investments in productive sectors resulted in inadequate maintenance of equipment and machinery and shortages in operating materials. This had a highly unfavourable impact on the Zambian economy (Cherv, 1989:136).[96] In the 1990s, the lack of reinvestment in the mining sector was considered the major reason for the poor performance of the ZCCM (according to research conducted by Kapika, Nyirenda & Mumba, 1996:8). Demand management programmes further contributed towards the considerable reduction of the labour force in the over-manned mining sector[97] and to a deterioration of social services, in particular health and educational facilities, also of the mining community (Cherv, 1989:136).

Moreover, the impact of the supply-side measures had a highly negative impact on the local support industries linked to the mining industry under government ownership of

[96] The allocation, from the government of only $290 million for the operations of the ZCCM in 1983, half of which went to service debts, was highly inadequate, since the ZCCM required at least $350 million in direct foreign exchange allocation in 1983 to sustain its operation and to pay for the essential debt service requirements it received (Cherv, 1989:128).

[97] The drastic increase in Zambia's foreign debt to $4 billion, by June 1984, of which $725 million was owed to the IMF and $350 million to the World Bank and with arrears alone to the IMF being around $100 million in 1986, which blocked the way to a new Standby agreement, forced the Kaunda government to introduce a massive retrenchment programme (Cherv, 1989:132).

the mines (Cherv, 1989:138). In particular, the decontrol of interest rates prescribed in 1985 led to a significant increase in interest rates. Moreover, the devaluation of the kwacha in 1983 and the currency's depreciation that accompanied the auctioning of the exchange rate in 1985[98] had a deleterious impact on the local support industries to the mines. Figure 4.12 shows that immediately following the first auctioning of the exchange rate in late 1985, the kwacha fell from US$1=ZK2.23 to US$1=ZK5.01 and dropped further to US$1=ZK12.7 in 1986 (McGrath & Whiteside, 1989:172).

The detrimental influence of the auctioning of the exchange rate and the consequent depreciation of the kwacha on the mining economy was largely owing to ensuing increases in the costs of imported inputs of Zambia's highly import-dependent backward-linked industries to the mining sector (Cherv, 1989:133). The high import content of local backward-linked industries to the mines, of about 50% and more, was mainly due to a general absence of domestic substitutes for intermediate and capital-intensive inputs. Accordingly, contrary to the argument of the IMF that the devaluation would encourage importers to switch to locally made input, the depreciation in the value of the kwacha in 1985 encouraged a vicious downward economic cycle.

More specifically, difficulties in obtaining more expensive spare parts and mining inputs and equipment[99] as a result of the high inflation following the devaluation and the depreciation of the kwacha especially in 1986 caused a drop in copper output. The consequent decline in foreign exchange earnings had a negative impact on employment, the balance of payments and government revenue that increased Zambia's debt burden. This spurred a further decline and shortage in the country's foreign exchange affecting an additional drop in the value of the kwacha (Cherv, 1989:128, 132, 136). Negative consequences as a result of the increases in the costs of mining inputs, in the context of the high import content of the local manufacturing sector, overrode the potential benefits of a weaker exchange rate for lowering *local* costs such as the costs of labour for the mining sector.

[98] Suspended from 24 January to 17 March 1987, but re-introduced again from 1995 under the Chiluba government.
[99] Such as spare parts, fuel and transport.

Subsequent to announcing a unilateral declaration of national bankruptcy, the Kaunda government abandoned the IMF policies of 1985. The declaration was precipitated by the country's enormous debt problem and declining foreign exchange, with virtually all of Zambia's export earnings (reaching only about US$650 million in 1985) having to be used to pay its debts of about US$400 million to the IMF, about US$71 million to the World Bank and nearly all of the rest for paying various donor countries (Cherv, 1989:134). Consequently, the government adopted its own government-devised strategy, the NERP, in 1987, discussed above (McGrath & Whiteside, 1989:178; Roberts, 1994, cited in Lungu & Silengo, 1997:15; Simutanyi, 1996:827; The Economist Intelligence Unit, 2002:5; Hanson & Hentz, 1999:484).

(*ii) IMF and World Bank policies adopted after the NERP – elaborated in the Policy Framework Paper (PFP), 1989-93*

After the NERP was abandoned, the Kaunda government was forced to adopt the market-oriented economic policies of the IMF, specified in the PFP covering the 1989 to 1993 period, and to follow performance 'benchmarks', detailed in the Rights Accumulation Programme (RAP) (Simutanyi, 1996:827; Hanson & Hentz, 1999:487). The SAPs instituted during that period essentially involved a devaluation of the currency, a decontrol of prices and the cutting of food subsidies (Simutanyi, 1996:827; Akwetey, 1994:56; Fraser & Lungu, 2007:9). Initially, the Kaunda government stayed on track with these policies,[100] but strayed from them in mid-1991.[101] The IMF then again suspended financial disbursements to Zambia (Hanson & Hentz, 1999:487; Simutanyi, 1996:828, 834; World Bank, 1996:10).

The depreciation of the kwacha, following the auctioning of the exchange rate, had a similar impact on the Zambian economy to what transpired in 1985-86, described above. The new pricing policy, aimed at encouraging greater movement of trade,[102] was an additional supply-side measure to those introduced before the NERP. The new pricing policy entailed the elimination of the import licensing system, the cutting of the

[100] Despite widespread riots in June 1990 during which 27 people were killed and hundreds were injured and arrested following the 100% increases in the prices of high-grade maize meal.

[101] Subsequent to the refusal of the IMF to allow for the postponement of a scheduled round of reduction of maize meal subsidies till after the first multi-party elections, in November 1991.

[102] Especially the decontrol of consumer goods, apart from maize.

maximum tariff rate, the simplification of the tariff structure and the removal of quantitative restrictions on imports and exports. Policies to encourage free trade in 1989 during Kaunda's government, in the context where the prices of consumer goods[103] were decontrolled, had a similar but less severe influence on the mining sector to what transpired with the introduction of trade liberalisation during Chiluba's government, discussed below.

4.2.2 Overview of the policies of the Chiluba government and the impact on the mining sector

In the beginning, the economic reform programme that the MMD government, which came into power in October-November 1991, negotiated and signed with the IMF did not differ significantly from those imposed on the Kaunda government in its first PFP. The first PFP in fact extended two years into MMD rule. However, the Chiluba government embraced all the measures in the stabilisation and adjustment package that the multilateral financial institutions advocated (Craig, 2002:2). It also executed the reform package more decisively and with greater commitment and coherence than the Kaunda government.[104] Subsequently, the SAPs that the Chiluba government accepted encompassed more far-reaching changes than those imposed on the Kaunda government.

The Chiluba government further distanced itself from its trade union support base and adopted foreign investor-friendly policies (The Economist Intelligence Unit, 2008b:4; World Bank, 2002b:28; Hanson & Hentz, 1999:487). This supports the argument of Bond and Manyanya (2002) that IMF and World Bank policies favour a realignment of government measures away from the workers. The Mwanawasa government adopted the neo-liberal policies and the privatisation of the state assets more cautiously than the Chiluba government had done.[105] It also reintroduced national planning policies (through the Planning Department at the Ministry of Finance) that the Chiluba

[103] Apart from maize.

[104] With the focus of the politics of adjustment in the Second Republic (1973-1991) being on whether to implement structural adjustment (Simutanyi, 1996:826).

[105] Interview with Fortune Kamusaki, 25 November 2003.

government had eliminated (The Economist Intelligence Unit, 2008b:5).[106]

Table A4 (in Annexure) lists the various stabilisation and adjustment policies that the Chiluba government adopted. Broadly, these policies entailed a more extensive and comprehensive liberalisation programme of the exchange and interest rates and of trade, as well as of stabilisation and structural reforms[107] such as the privatisation of state-led sectors (World Bank, 2002a:18, 2002b:27, 28; Simutanyi, 1996:829; Ministry of Mines and Mineral Development, 2003:2). By early 1993, all controls over prices, interest rates, foreign exchange rates and foreign currency allocations had been removed and subsidies eliminated (Craig, 2002:2). The acceptance of the RAP led to almost US$1 billion in aid flowing into Zambia annually, during 1991-96 (Hanson & Hentz, 1999:488).

The effect of the Chiluba government's liberalisation and industrial policies on the local support industries to the mining sector is considered below. This is followed by a brief contextualisation of the privatisation of the mines in Zambia.

4.2.2.1 <u>Impact of liberalisation policies and weak industrial policies of the Chiluba government on the support industries to the mining sector</u>

The liberalisation policies that the MMD government adopted, promoted by the IMF and the World Bank, considered below, include the liberalisation of the foreign exchange, interest rates and of trade policies.

(i) The liberalisation of the foreign exchange and interest rate

The Chiluba government's more rigorous and extensive adoption of liberal policies of the foreign exchange (following the abolishment of the Exchange Control Act in 1994) and of the financial market had a similar but more severe effect on local support industries to the mines than what transpired with the auctioning of these markets under Kaunda's government, from 1985 to 1986. In sum, the depreciation of the kwacha and

[106] Interviews with Silane Mwenechanya, 24 October 2003 and Ladslous Mwansa, 7 October 2003.
[107] Partly because consensus existed among the main groups on the necessity for structural adjustment (Simutanyi, 1996:826).

the high increases and volatility in the interest rate[108] (that rendered lending inaccessible to many local entrepreneurs)[109] that respectively accompanied the liberalisation of the exchange rate and of the financial markets, reduced the capacities of the local support industries to the mining sector (The Economist Intelligence Unit, 2002:32; World Bank, 2002a:14, 2002b:6). This is well reflected in the steep decline in the growth of manufacturing and in its contribution to GDP, illustrated in Figures 4.3, 4.4 and 4.5. As was the case in the 1980s, their flawed structure prevented the local backward-linked industries to the mining sector from taking advantage of the potential incentive pertaining to the depreciation of the local currency, to procure locally.

On the contrary, in the context of a poorly integrated local manufacturing sector, on an inter-industry level and of its high import content,[110] the significant increases in inflation due to rises in the costs of imported intermediate inputs, following the depreciation of the local currency, undermined the development of many locally-based manufacturing companies. Accordingly, rather than encouraging local industrial development the impact of the high inflation following the depreciation of the local currency was subsequently expressed in a macro-economic meltdown. Greater linkages of Zambia's industries that would have reduced their dependence on imports for intermediary goods should have been introduced before the liberalisation policies were implemented, for ensuring a more beneficial impact on local capacities from the depreciation of the local currency.

(ii) Free trade policies

The exposure of the Zambian economy to full-scale trade liberalisation policies before the mines were privatised and at a time when the local support industries to the mines were weak, encouraged the import of superior technology and lower priced, higher

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[108] Caused by linking the determination of nominal interest rates for both the borrowing and the lending rates to the sale of Treasury Bills (TB) in the TB market, from March 1993, the devaluation of the kwacha and the rampant inflation rate, the result largely of the policy of monetary authorities under Chiluba's rule to allow the kwacha to depreciate for a time with a periodic tightening of its monetary stance.

[109] A low interest rate is one of the essential ingredients together with an explicit and coherent domestic investment strategy, strong financial institutions, capital and entrepreneurship, for ensuring more beneficial outcomes from trade liberalisation, according to Rodrik (1999:19).

[110] Interview with Chama Kapambwe, 11 November 2003.

quality and better packaged mining inputs[111] from more competitive foreign companies. Especially inputs from South Africa and Zimbabwe[112] flooded the Zambian market (Africa Analysis, 2002a:20; Africa Research Bulletin, 2001a:14627, 2002a:15037; The Economist Intelligence Unit, 2002:27, 48, 49; ZPA, 2000b:16).[113] Before the liberalisation of trade, local industries enjoyed considerable benefits under the protectionist policies of the Kaunda government, though limited mainly to less capital-intensive goods (World Bank, 2002b:29; SADC, 2000:346; Singogo, 2000:11, 12).[114]

While the greater competitiveness that free trade policies introduced benefited the copper mines in Zambia, the associated reduction in the domestic demand for locally produced inputs to the mines had a highly negative influence on the local and locally-based industries and suppliers to the mines.[115] By the mid-1990s, over 60% of inputs for manufacturing, comprising mainly of capital goods,[116] were imported.[117] The free trade policies, alongside the decontrol in the price of consumer goods[118] and the high costs of imported inputs in the manufacturing sector in Zambia, linked to the depreciation of the kwacha, further encouraged a switch from importing capital equipment to the trading of cheaper imported consumer goods. The switch led to a stagnation in the imports of capital goods, required as intermediary inputs to local industrial companies, which undermined the manufacturing sector, especially the backward-linked industries to the mining sector (Craig, 2001:2; World Bank, 2002b:28).

A myriad of especially engineering support industries to the mining sector closed down as a consequence of trade liberalisation, contributing to the stagnation of Ndola, which before trade liberalisation had been a vibrant industrial city. The engineering companies linked to the mining sector that closed down included Gencore, Lusaka Engineering Industries, DHS Engineering, Lancore Engineering, African Explosives and the BP

111 Interview with Fred Yamba, 25 November 2003.
112 Australian, UK and USA companies are also moving into the Zambian market.
113 Interview with Honourable Dipak Patel, 15 October 2003.
114 Since most capital-intensive technologies were imported despite import substitution policies (Leistner, 1996:11.13-11.14, 20; Makgetla, 1994:107, 109).
115 Interview with Stuart Cruickshank, 28 October 2003.
116 And 25% for consumption goods, such as food, beverages and tobacco.
117 The Dunlop plant in Zambia then imported about 90% of their inputs (Leistner, 1996:11.14).
118 Apart from maize.

lubricant plant.[119] Various producers of tyres, namely Dunlop, Buffalo and Consolidated Tyre Services, that had previously supported the mining sector, also closed down in Zambia.[120, 121]

(iii) Industrial policies of the Chiluba government

Contrary to the protectionist policies of the Kaunda government,[122] in addition to liberal policies the weaknesses in the industrial policies of the Chiluba government also adversely affected the local backward-linked industries to the mining sector. Table A7 (in Annexure) lists and elaborates on the major factors prior[123] and subsequent to the privatisation of the mines during MMD rule that undermined the capacities of local industries and suppliers to the mining sector.

Main weaknesses in the industrial policies of the MMD government that negatively affected local suppliers included: (i) a failure to provide appropriate safety nets to protect local suppliers and manufacturers against the negative consequences of privatisation; (ii) a lack of active government participation to encourage the competitiveness of local companies, among others through adequate training, before trade liberalisation policies were introduced; (iii) the absence of greater government participation in the development of the manufacturing sector, through an effective industrial policy (to also develop backward and forward linkages to mining); (iv) increases in duties on raw materials over finished goods that encouraged local suppliers to switch from production to the trading of goods; and (v) the provision of extensive incentives, including lower taxes and concessions, to foreign investors not extended to local investors (effectively subsidising foreign investors).

Additional factors that adversely influenced local industries were the lack of capital, the

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[119] Interviews with Andrew Sardanis, 19 October 2003; Eddy Kapungulya, 13 November 2003; Honourable Dipak Patel, 15 October 2003; Honourable Eugene Appel, 24 November 2003; Isaac Masonda, 11 November 2003; Fortune Kamusaki, 25 November 2003; Charles Muchimba, 18 November 2003; John Lungu, 12 November 2003; David Chilipamushi, 20 October 2003 and Fred M'muembe, 14 October 2003.

[120] While consolidating or relocating their plants mainly to South Africa and/or Zimbabwe.

[121] Interviews with Eddy Kapungulya, 13 November 2003; Wilphred Katoto, 12 November 2003; Fred M'muembe, 14 October 2003 and John Kangwa, 21 November 2003.

[122] Through import substitution and through the establishment of state-owned manufacturing companies that boosted the manufacturing capacity of Zambia.

[123] Mainly from 1995 to 1999.

high production costs of locally-based manufacturing companies, the weak domestic market and the lack of an aggressive marketing campaign of local suppliers to the mines. Main factors accounting for the high costs of local production entailed: (i) the increases in the interest rates, following the introduction of a liberal financial market and the delays in the ZCCM paying its debt to local suppliers; (ii) cost-push inflation introduced onto the Zambian economy that augmented the price of imported mining inputs, subsequent to the depreciation of the kwacha; (iii) higher taxes imposed on local businesses over foreign businesses; (iv) the high costs of transportation, petroleum fuel and of electricity; (v) outdated equipment; and (vi) poorly maintained assets.

The above discussion shows that the poor industrial policies of the Chiluba government, favouring liberal policies and foreign investor-friendly policies, had a highly detrimental impact on the local backward linkages to the mining sector. In the context of the weak local industries and the highly imperfect markets, Zambian industries could not compete with more competitive international companies, following the introduction of trade liberalisation policies before the mines were privatised. This precluded local industries from benefiting more from the improved performance of the mines under private ownership. The negative impact of the liberalisation policies and poor industrial policies on the Zambian economy are also reflected in Figure 4.5 that shows a huge decline in the contribution to the manufacturing sector to GDP from 37.2% in 1992, 27.9% in 1993 to only 11.24% in 1994. Moreover, Figure 4.7 shows a considerable decline in manufacturing employment during the 1990s, dropping significantly by 29 400 from 1991 to 1999, from 75 400 in 1991 to 46 000 in 1999, mainly as a result of the introduction of trade liberalisation policies in Zambia.[124]

When a country moves from low productivity towards zero productivity, which was the case with the bankruptcies of many backward-linked companies to the mining sector, especially following the introduction of trade liberalisation policies in the 1990s, it reduces the benefits to the country (Stiglitz, 2002:59). Additionally, the lack of government assistance to local manufacturing companies during Chiluba's rule, whilst

[124] Interview with Stuart Cruickshank, 28 October 2003.

encouraging foreign investors, is contrary to the policies of developmental states that encourage state-directed investments (Leftwich, 1995:410). Successful industrial policies, involving strong and effective government intervention, were crucial to the phenomenal development of developmental states, according to Amsden (1997:469, 470).

4.2.2.2 Privatisation policies of the mines in context

A detailed exposition of the privatisation of the copper mining sector in Zambia is provided in Chapter 5. The discussion below merely contextualises the issues that informed the privatisation of the mining sector.

Instead of negotiating from a strong bargaining position, crucial in the case of the mining sector to ensure that the greatest share of the rent element expected to collect major returns accrued to the government, the Chiluba government bargained from a weak position in the privatisation of the mines. This was especially the case with the privatisation of the final but more lucrative mines, viz. the KCM and the Mopani Copper Mines (MCM). The poor bargaining leverage of the Chiluba government prior to the decision to unbundle the mining sector, prevented the government from setting the terms for the privatisation of the ZCCM, selecting options for privatising the ZCCM and determining to whom and the form in which the ZCCM would be sold, and the terms of the sales. Various pressures that the mining sector faced that weakened the bargaining position of the government were paramount in precipitating the privatisation of especially the remaining mining assets.

The principal factors that precipitated the privatisation of the final mines, elaborated upon in Table A6 (in Annexure), were, broadly: the poor economic position of the ZCCM and of the Zambian economy; pressure from suppliers and donors (who linked balance of payment funds to the privatisation of the mines); unfavourable external factors, namely socio-political instability if the ZCCM were to liquidate and the decline in the price of copper; and certain strategies of the TNCs. The poor economic position of the Zambian economy and of the ZCCM in the late 1990s immediately prior to the privatisation of the final mines significantly reduced the bargaining leverage of the government. The poor economic performance of the country was mainly due to the huge losses of the ZCCM. The losses were largely as a result of the lack of recapitalisation of the mining company and the enormous increases in the debt of the government and loan obligations (partly due to the state's assumption of the debt of various majority SOEs – including that of the ZCCM). The country's declining foreign exchange and tax revenue, pressure from suppliers and shortages of supplies added to the economic difficulties that the ZCCM experienced at the time.

The interaction of multiple factors and actors, in particular foreign actors such as the donors (including the World Bank and the IMF), foreign consultants and the potential foreign buyers of the mines, greatly influenced the options selected for privatising the mining industry, the form that it would take and its enforcement. Especially AAC, as a minority shareholder of the ZCCM and because of the pre-emptive rights it enjoyed, played a pivotal role in determining the options that the government adopted for privatising the ZCCM. Accordingly, contrary to developmental states where the government possesses a corporatist role in setting policies independent of international financial institutions, in the context of a weak state the Chiluba government largely accepted and followed the IMF and World Bank policies, also in the privatisation of the ZCCM. Such a position undermined a greater corporatist role for the state. The influences of privatisation policies and of the majority control of TNCs in mining companies on the Zambian economy are examined in detail respectively, in Chapters 5 and 6.

4.3 THE REDISTRIBUTION OF MINING RESOURCES AND THE IMPACT ON DEVELOPMENT AND ON THE POLITICAL ECONOMY OF ZAMBIA

The dissimilar policies of the Federation and the Kaunda and Chiluba governments had different consequences on the reallocation of the resources of mining on the Zambian economy, with different political-economic implications for the various stakeholders that are investigated below. The brief overview of the redistribution of the resources of the mining sector and the impact on the Zambian economy during the pre-independence period serves as a standard against which the redistribution of the mining resources under government ownership is evaluated.

4.3.1 The pre-independence period

During the Federation years in the 1950s until independence, the transfer of substantial tax revenue and foreign exchange resources from Zambia mainly for the development of the rest of the Federation, especially Southern Rhodesia (present-day Zimbabwe), proved detrimental to the development of Zambia. From 23 October 1953 to independence in 1964, about £97 million was repatriated out of Zambia, in lost taxes to Zambia. Much of the savings and salaries of the expatriate community also left Zambia before independence (Turok, 1989:28, 36). Furthermore, the externally oriented consumption policies of the short-term contract mining staff and of the inputs for the copper industry, such as oil, coal and other essential goods, which encouraged the importation of goods mainly from Southern Rhodesia, hindered the development of especially the backward-linked industries to the mining sector.

Notwithstanding the well-developed modern and technologically sophisticated mining sector infrastructure that the Kaunda government inherited at independence, the failure under colonial rule to redistribute surpluses from mining for the development of the local economy contributed towards the stagnation of the rest of the Zambian economy. In particular, wage employment in Zambia remained at 270 000 throughout the pre-independence period, and the private sector and the manufacturing base in Zambia were small and undeveloped. Manufacturing contributed only 7% to GDP at independence (Turok, 1989:28, 36, 39, 44; Cherv, 1989:127).

During the Federation years, the redistribution of a portion of surpluses from mining (then the largest single industry in the Federation) to mining employees and managers, partly through the provision of social services such as schools and hospitals (owned by the mines) and of housing,[125] were confined to the expatriate population. In contrast, the indigenous Zambians benefited very little from the copper mining industry (MUZ,

[125] Interview with Silane Mwenechanya, 24 October 2003.

1994:1; Seidman, 1977:218).[126] The health and educational infrastructure of the indigenous Zambians was poorly developed during the colonial years. At independence, less than 0.5% of the Zambian population had completed their primary education and Zambia had only 107 graduates (Fraser & Lungu, 2007:7).

4.3.2 The Kaunda era

In contrast to the externally oriented mining policies and consumption patterns of the Federal government,[127] favouring mainly the expatriate community and Southern Rhodesia, electoral-maximising motives during Kaunda's government encouraged a much wider redistribution of the surpluses from copper mining to the Zambian economy. Under Kaunda's government, mining revenue was also spent on non-core mining activities and non-mining sectors and businesses,[128] enabled through the direct ownership and control of the government in mining parastatals since 1974 (Maambo, 1998:Figs. 8, 9; MUZ, 1994:4). The non-core mining activities and non-mining sectors developed from surpluses of the mining companies included rural development, import substitution, the introduction of subsidies, export promotion, industrialisation and the development of infrastructure of Zambia, and the social service infrastructure of the mining community (MUZ, 1994:4; World Bank, 1996:8).[129] In particular, surpluses from mining were used for extending the provision of a wide range of new services[130] to the hitherto neglected African majority.

Additionally, mining revenue was employed to encourage the growth of economic and social activities that were dependent on the miners' income, such as industrial activities, the establishment of shops and the buying of land for farming[131] to supply food to the

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126 Interview with Sipho Phiri and Simon Capper, 30 October 2003.

127 Namely, policies to externalise Zambia's mining resources for the development of Southern Rhodesia, and practices that encouraged the repatriation of profits of mining TNCs out of Zambia.

128 Such as tourism, freight and forwarding, dry cleaning, public transportation (also air travel) companies and the operations of the mills, after they were nationalised, following huge increases in the prices of mealie meal and subsequent food riots in 1986 (interviews with Andrew Sardanis, 19 October 2003; Charles Muchimba, 18 November 2003; Zion Simwanza, December 2003; Danny Kalyalya, 31 October 2003; Fred M'muembe, 14 October 2003 and M. Shandavu, 10 October 2003).

129 The deployment of resources from the mining sector to develop non-mining related activities was precipitated by a shortage of private investment (attributable mainly to unfavourable fiscal policies and rigid exchange control regulations) and the poor performance of the subsidised SOEs, which pervaded the Zambian economy (MUZ, 1994:4; World Bank, 1996:8, 2003b:135).

130 Especially social services.

131 That culminated into the establishment of one of the biggest farms in Zambia, the Mpongwe farming scheme, a highly successful operation at the time (interview with Willie Sweta, 30 October 2003).

mining community (Fraser & Lungu, 2007:8; World Bank, 2004a:11).[132] Proceeds from copper production were further diverted to less productive sectors[133] and for political purposes, such as running the affairs of the party and paying Zambia's foreign debts.[134] The spending of mining revenue on non-mining related businesses and in particular on less productive sectors proved detrimental to the development of the mining companies, especially when revenue from mining became scarcer. These activities limited reinvestment in the mines that is so crucial to sustaining the mining sector.

Especially in the first decade of independence, the reallocation of surpluses from mining during Kaunda's government, much of which were repatriated out of the country before independence, to develop other sectors of the economy was central in promoting the notable development of the Zambian economy (Turok, 1989:41; Fraser & Lungu, 2007:8). The wider redistribution of mining revenue for developing the social services and the manufacturing sector of Zambia under Kaunda's government, from the pre-independence period, which were instrumental in the notable development in these areas, are explored in greater detail below.

4.3.2.1 <u>The development of social services</u>

The philosophy of 'Zambian humanism', focusing on developing the potential of the indigenous population, motivated the decision to develop the social service provision of Zambians during Kaunda's government. The Zambianisation policies, the five-year National Development Plans,[135] the extension of the 'cradle to grave' welfare policy, (confined to the expatriate population under private ownership of the mines before independence) to the majority African population[136] were the main government policies employed to promote 'Zambian humanism'. The 'cradle to grave' welfare policy

[132] Interviews with Bernadette Mwakacheya, 17 October 2003; Zion Simwanza, December 2003 and Fred M'muembe, 14 October 2003.

[133] Such as the buying of the Challenger Jet (interviews with Sipho Phiri, 30 October 2003 and Thomas Kabandama, 13 November 2003).

[134] Interviews with Fortune Kamusaki, 25 November 2003; Francis Kaunda, 20 October 2003; Dave Phiri, 23 October 2003; Willie Sweta, 30 October 2003; Chama Kapambwe, 11 November 2003; Dennis Wood, 21 October 2003; Andrew Sardanis, 19 October 2003; Valentine Chitalu, 22 October 2003; John Lungu, 12 November 2003 and Thomas Kabandama, 13 November 2003 and M. Shandavu, 10 October 2003.

[135] Policies of the National Development Plans that promoted 'Zambian humanism' through directing the profits of the nationalised copper mines also to the building of hospitals, schools and universities and in the provision of subsidies to state-owned manufacturing companies and to consumers.

[136] Interviews with David Chilipamushi, 20 October 2003 and Fred M'muembe, 14 October 2003.

involved the employment of revenue from the mining sector to develop also the non-core activities of the mines and to provide various incentives, such as social services and employment benefits to mining employees (Lungu & Silengo, 1997:12, 36; Seidman, 1977:224; World Bank, 1996:8).

The employment of mining surpluses to extend social services to local Zambians as well, led to huge improvements in the provision of social services of the indigenous mining community. Policies of 'Zambian humanism', in particular the Zambianisation policies, further enabled the indigenous Zambians greater participation in the modern sector and were effective in redressing the highly uneven distribution of income and wealth that disadvantaged the locals. At independence, the social indicators of indigenous Zambians were among the lowest in the world (World Bank, 1996:8).

In addition to taking care of their workers, revenue from mining was also employed to provide social services to the whole mining community.[137] The social services provided to mineworkers and their families included the provision of free education for miners' children (also at university level)[138] and mineworkers were provided with subsidised housing, food, electricity, water and transport (Fraser & Lungu, 2007:8). In 1971, current expenditures for education increased five-fold from the immediate pre-independence period to US$83 million, over 12% of the budget (Seidman, 1977:224; MUZ, 1994:2). In 1986, the Copperbelt University (Zambia's second university) was established.[139] The development of the human capital of local Zambians through the state-sponsored training of Zambians, and crucial to the Zambianisation policy, proved a highly successful programme. However, it was severely eroded under private ownership of the mines (Lungu & Silengo, 1997:12, 21, 36; Seidman, 1977:224; SADC, 2000:349).[140]

Moreover, funds for health multiplied seven times in 1971 from 1963, to US$37

[137] Such as managing the environment, maintaining the roads, collecting refuse, as well as establishing cafeterias, bars and social clubs, including, Youth Development Schemes, women's clubs and social casework agencies that supplied relevant services, under their competence, to the mining community in the mining townships.
[138] Interviews with Alick Lungu, 14 October 2003 and Bernadette Mwakacheya, 17 October 2003.
[139] Interviews with John Lungu, 12 November 2003 and Honourable Captain Moono, 2 December 2003.
[140] Interviews with Sipho Phiri, 30 October 2003; Fred M'muembe, 14 October 2003 and Dennis Wood, 21 October 2003.

million, representing over 5% of the budget (Seidman, 1977:224). Effective healthcare was provided for the mining community, with hospitals[141] being established in all mining settlements,[142] also at Nchanga and Konkola, where no government hospitals had previously existed. The mining companies further provided recreation clubs for employees (Fraser & Lungu, 2007:8).[143]

Furthermore, electoral-maximising motives account for the much higher number of employees employed in the mining sector under state ownership during Kaunda's government than under private ownership (refer to Figure 4.7).[144] The high employment levels and the provision of social services, however, became unsustainable in later years. The unprecedented boom in the world copper prices and the increasing output of copper (which pushed the national product upwards to the exceptionally high annual rate of 12%) in the early 1970s then enabled the redistribution of surpluses from mining under Kaunda's government.

4.3.2.2 <u>The development of the manufacturing sector</u>

Policies aimed at redistributing surpluses and taxes from mining to develop Zambia's manufacturing sector (which was almost non-existent at independence), mainly the parastatal manufacturing sector, had a highly positive impact on the development of this sector. The development of the manufacturing sector also promoted a greater diversification of the economy than what was the case during the pre-independence period. Accordingly, under Kaunda's government, the performance of the highly import-dependent manufacturing sector became strongly linked to that of the mining sector[145] as the dominant contributor of Zambia's foreign exchange (Turok, 1989:43; McGrath & Whiteside, 1989:172, 173; Fraser & Lungu, 2007:7, 8).[146]

The manufacturing sector was largely nurtured through industrial policies entailing the

[141] With competent medical personnel.
[142] That resulted into the ZCCM having one or two hospitals at each of its operating divisions.
[143] Interviews with John Lungu, 12 November 2003 and Honourable Captain Moono, 2 December 2003.
[144] Interview with Willie Sweta, 30 October 2003.
[145] Such as textiles, food processing, tobacco and chemicals.
[146] Interview with Silane Mwenechanya, 24 October 2003.

Import Substitution Industrialisation (ISI) policies[147] that the Kaunda government introduced between 1965 and 1980 and the development of the parastatal sector. The parastatal sector was primarily built in the first decade of independence, from 1964-74, mainly from the revenue from mining. The state played a direct role in promoting both of these policies (Craig, 2002:1). The state also entered into joint ventures with foreign corporations to establish a range of new industries as part of the parastatal sector (Craig, 2002:1; World Bank, 1996:9).

The policy of the Kaunda government to take over control of most foreign-owned businesses, including large private companies,[148] while leaving some economic space for Zambian entrepreneurs in small- and medium-sized concerns, led to the Zambian economy becoming a mixed-economy with a strong state sector from the 1970s (Turok, 1989:44). The government established both the Industrial Development Corporation (of Zambia) (INDECO), the state holding company for manufacturing and the ZIMCO, the controlling or master holding company for parastatals, to expand the share of the state sector in productive activities (World Bank, 1996:9). By the mid-1970s, most of the main enterprises in the economy were under state ownership, held within a hierarchy of state holding companies, with ZIMCO at the top (Craig, 2002:2).

The manufacturing sector grew phenomenally under the state-led industrialisation initiatives of the Kaunda government, sponsored from mining revenue, with ZIMCO becoming a formidable parastatal in the 1970s, ranking by turnover in 1980 in the first 100 companies in the world outside the United States. In 1975, the assets of ZIMCO added up to ZK1 468 million and total government-controlled assets reached almost ZK2 000 million (ZIMCO, cited in Turok, 1989:44). About 75% of the total assets of ZIMCO, amounting to ZK713 million in 1971, were obtained from the copper mines. This underscores the pivotal role that the mining sector played in developing the manufacturing sector during Kaunda's government (Turok, 1989:44).

Moreover, INDECO, that became the main vehicle for state-led industrialisation, also of

[147] ISI policies benefited mainly the high-income bracket (Turok, 1989:41).
[148] Such as insurance companies and building societies and industries.

backward linkages to the mining sector, rapidly established itself under the directive of Andrew Sardanis[149] as a strong force in the economy. This was achieved through the state's taking over responsibility for the management of its minority interests in associated companies and of those enterprises and corporations within which it held the majority shares. The assets of INDECO increased seven-fold; from 1965-67 and by 1971 the total state-controlled assets amounted roughly to ZK1 009 million. Agreements established by INDECO with international foreign investors such as Japan, Italy, Britain, America and South Africa, led to the establishment of various enterprises, including backward linkages to the mining sector, such as an explosives factory, a tyre factory, cement works and other enterprises in Zambia[150] (Turok, 1989:40).

Accordingly, the manufacturing sector, which was almost non-existent at independence, grew rapidly in the first decade of Kaunda's rule[151] from only about 7% of Zambia's GDP in 1964 to 12.1% in 1974[152] and Zambia's overall GDP increased by an average of 6.1% per annum, amongst the highest in Africa (Cherv, 1989:126). Under Kaunda's government, the manufacturing sector continued to grow, reaching 36% of Zambia's GDP in 1990.[153] Employment in manufacturing grew by 77% over the 1964-69 period, output grew by 192% in nominal terms or by 60% in real terms, from 1965 to 1970 and gross fixed capital formation grew by 472%, from 1964 to 1968 (Young, 1973, cited in Turok, 1989:43, 44). The phenomenal state-led manufacturing growth during Kaunda's government, mainly from the revenue from mining, accentuates the powerful role that interventionist industrial policies could potentially play in promoting industrialisation.
Additionally, the highly negative influence that trade liberalisation policies had on the Zambian-based backward-linked industries to mining in the 1990s further illustrates the importance of effective industrial policies of the government in promoting industrialisation in developing countries.

However, despite the impressive growth in the manufacturing sector in comparison to

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149 Then Chief Executive of INDECO.
150 For example, a fertiliser factory, a sugar estate, a textile mill and hotels.
151 Interview with David Chilipamushi, 20 October 2003.
152 Using constant 1977 prices.
153 If 2000 constant prices are used.

that of the Federation years, most of the mining inputs, comprising largely of capital goods, were still imported. The poor integration of the mining sector to the local manufacturing sector, mainly owing to the confinement of most of the industries to the production of consumption rather than intermediate or capital goods, largely accounted for the high import content of the mining sector (Saasa, 1987:10). The failure of the mining sector to develop significant local backward and forward linkages and the high import content of almost 50% of most of the few existing local backward-linked industries to the mining industry[154] during the pre-reform period, also reduced the impetus of the mining sector to evolve as an engine of growth for other sectors. Instead, the mining sector developed as an enclave surrounded by less developed sectors and a very backward agricultural sector that the Kaunda government tended to neglect (World Bank, 1996:9, 10; Saasa, 1987:11). By the mid-1970s, the manufacturing sector of Zambia was still a heavily protected state-led industrial sector.

Furthermore, despite significant growth in the Zambian manufacturing sector during Kaunda's government, the uncompetitive practices of the protected parastatal-dominated manufacturing sector generated inefficient companies, with high consumer prices, low productivity and relatively poor quality of goods and services. The protection provided to the parastatal industries further disadvantaged private sector businesses. While the parastatal sectors performed well in the 1960s and 1970s, losses were subsequently experienced in many of these public enterprises, estimated at US$455 million from 1985 to 1989 (World Bank, 2002b:5). In the latter part of Kaunda's rule, controls imposed on the foreign exchange allocations to suppliers, due to a scarcity of foreign exchange, further disadvantaged the Zambian suppliers to the mines. As a result of huge inefficiencies, many local support industries to the mining sector became bankrupt with the lifting of controls and with the full-scale introduction of trade liberalisation policies in the 1990s, discussed above in Section 4.2.2.1 (World Bank, 1996:9, 2002b:27).

Accordingly, interventionist industrial policies, whilst necessary, are not sufficient in

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[154] Such as machinery, electricity, water, foundries and metal products and distribution.

promoting the development of competitive local industries. In the absence of setting strict targets that local industries had to meet, which would have helped infant industries to grow up and become internationally competitive, protectionist policies promoted the emergence of several 'lame ducks' that drained Zambia of its resources and obstructed sustainable growth in the manufacturing sector. In contrast, the formidable development of South Korean industries was nurtured through interventionist policies, as well as through the setting of strict benchmarks that manufacturers had to meet to become internationally competitive,[155] before the economy was opened to foreign companies (Evans, 1998; Padayachee, 1995:173).

4.3.2.3 Political-economic implications of Kaunda's mining policies

Under government ownership of the mines during Kaunda's government, the significant redistribution of revenue from mining for expanding and developing the social amenities of Zambia and for encouraging Zambianisation promoted the interests of the Zambian population. The policies that ensured that the mines were being managed mostly by Zambians, at chief executive, senior management and the technical levels[156] and that promoted the human capital development of local Zambians were highly favourable to Zambian mineworkers and managers.[157] Expatriates were largely sidelined by Zambianisation policies. The building of local infrastructure from mining revenue also contributed considerably to national development.

Additionally, industrial policies, through the protectionist policies that Kaunda's government introduced that contributed considerably to the development of the local manufacturing sector, were favourable to local entrepreneurs. However, the emergence of several 'lame ducks', mainly owing to the failure of the government to increase the global competitiveness of local entrepreneurs alongside protectionist policies, constituted a drain on Zambia. The failure to establish more local backward and forward linkages to the mining sector and to lower the import content of manufacturers further

[155] A distinctive feature of Korea lies in the discipline the state exercised over private firms and represented an integral part of the vision of the Park government (Amsden, 1998:14).
[156] Interview with Willie Sweta, 30 October 2003.
[157] Expatriates were, however, also employed in some technical positions. For instance, the Cost Accountant and the Chief Geologist at the ZCCM were expatriates (interviews with L. M. Lishomwa, 29 October 2003 and Willie Sweta, 30 October 2003).

limited the development of local manufacturing industries.

The omission to establish these measures also obstructed sustainable growth in the manufacturing sector. This was demonstrated in the collapse of many industries following the introduction of trade liberalisation policies. The redistributive activities of the Kaunda government, to fulfil political or electoral-maximising objectives, were also unsustainable in the context of the negative impact that the over-extension of the resources of the ZCCM and the associated increasing costs of production of the mines had on the performance of the ZCCM.

4.3.3 The period of Chiluba's government, during government ownership of the mines

It has been noted in Section 4.2.2.1 above that the more extensive and comprehensive liberalisation programme of trade, of the exchange rates and of the financial markets that the Chiluba government adopted, as well as the poor industrial policies that it instituted in the 1990s, disadvantaged the local support businesses to the mining sector. In particular, the higher production costs of local suppliers, linked to the more rigorous re-introduction of supply measures from 1995 under the Chiluba administration (namely the auctioning of the interest and exchange rates), in the context of the high import content of the local industries, had an adverse impact on the local suppliers. The bankruptcies of many locally-based industries and the backward-linked industries to the mines as a result of the stricter adoption of trade liberalisation further disadvantaged the Zambian-based industries. Conversely, the liberal and foreign investor-friendly policies mainly benefited the mining TNCs that gained from cheaper, better quality imported inputs. Such policies also favoured foreign, especially South African backward-linked companies that increasingly supplied inputs to the Zambian mines.

Consequent reductions in the output of locally-based industries and in the employment levels of Zambia also had a negative impact on the Zambian workers and the economy. Moreover, certain demand management programmes of the IMF and the World Bank in the 1990s and under private ownership of the mines required for improving the budget deficit of the government, further disadvantaged the Zambian workers that were retrenched in 1990s. In addition, the demand management measures degraded the social services of the Zambian community. The political-economic consequences of the privatisation policies in the mining sector and of the majority control of TNCs over mining are discussed in detail in Chapters 5 and 6.

In summary, in the longer run, in the absence of economic growth and greater reinvestment in the mining sector, the Kaunda government's approach of employing the mining sector as the 'cash cow' of the economy contributed significantly from the 1980s towards degrading the global competitiveness of the mining sector. It further undermined the performance of the mining sector, precluding a greater redistribution of resources from that sector. This suggests that economic growth is a prerequisite for sustainable redistribution. Without growth, the redistributive activities into unproductive sectors of the economy in fact undermined growth.

4.4 ECONOMIC INDICATORS

Several economic indicators are reviewed in this section in order to gain insight into the effects of different variables, such as changes in ownership, mining policies of the governments and the policies of the IMF and the World Bank, on the Zambian economy and in particular on the mining sector. The influence of diverse factors on the trends of various economic indicators is also exposed in the investigation. Furthermore, an examination of the trends provides evidence as to whether the data match theoretical arguments considered in this study. The position of Zambia's copper mining sector in the international context is considered first. Several national economic indicators are then examined, followed by those more specific to the mining sector.

4.4.1 Position of Zambia's copper mining sector in the international context

The role of the copper mining sector in Zambia in the international context is considered, briefly, in terms of its international cost and production competitiveness.

4.4.1.1 International cost competitiveness of the copper mining sector

In contrast to its competitors, including CODELCO (the majority state-owned copper company in Chile), the copper industry in Zambia that once set the pace for the world's copper mining industry[158] and was one of the world's lowest cost producers, became decidedly less cost competitive, especially in the 1990s. The steady increase in the cost of copper production in Zambia,[159] beyond those of most of its global competitors, despite the Copperbelt having some of the largest copper and cobalt deposits in the world, rendered the profitability of the Zambian mines more vulnerable to the international slump in base metal prices. Base metal prices were particularly depressed in the late 1990s (World Bank, 2003b:135, 2004a:3; The Economist Intelligence Unit, 2002:39). However, the mining industry started to lose its global market share as early as 1982, when the NCCM and the RCM merged to form the ZCCM (Kapika *et al*., 1996:8).

While the major producers of the world produced copper at a cost in 2003 of between US$0.30/lb and US$0.45/lb,[160] with the most efficient mines producing at a cost of production below US$0.10/lb,[161] the weighted average cost of copper production of Zambia was US$0.58/lb (World Bank, 2003b:135). This placed the country in 2003 in the 85th percentile in the world; a modest improvement over the status of the cost competitiveness of the ZCCM in 1995, just prior to the privatisation of the mines, when it reached the 95th percentile. The high costs of production of several mines in Zambia (including Konkola and Nkana, the country's most prolific mines), of about US$1.17 per pound in early 2000 relegated these mines to amongst the highest-cost producers in the world (World Bank, 2002b:15, 2004a:48; ZPA, 2000c:34).

These high production costs render Zambia's copper mines highly uncompetitive globally (World Bank, 2003b:135). A persistent high cost of production, above that of

158 Interview with David Chilipamushi, 20 October 2003.

159 In 1997, an estimate of over US$2 billion in capital expenditures were required to maintain copper production merely at existing levels (Maambo, 1998:Fig. 9).

160 Interview with Silane Mwenechanya, 24 October 2003.

161 According to a recent international study, comparing the cash costs of copper production per pound and which covered 95 copper mines, accounting for 83% of the world's production.

the average world market, alongside the trend of declining international copper prices,[162] would cause the copper industry in Zambia to become unsustainable, demonstrating the precarious position of the industry (World Bank, 2003b:135, 136, 2004a:48). The factors that contributed to the high costs of copper production are elaborated upon in Section 5.4.1.1 of Chapter 5.

4.4.1.2 International production competitiveness of copper mining

In the late 1960s and in the 1970s, Zambia was among the top global copper producers and the envy of CODELCO, boasting production levels of over 700 000 tons in 1969. At independence, Zambia supplied a tenth of the world's copper. However, while the output levels of its competitors, particularly Chile, continue to rise, the production levels of Zambia have dropped progressively, especially from the 1980s (The Economist Intelligence Unit, 2002:40; Seidman, 1977:218). In 1996, CODELCO produced about 1 million tons of copper per annum, outstripping by far production at the ZCCM that then fell to 313 900 tons (Kapika *et al*., 1996:7). In 2003, the production levels of copper in Chile reached about 4 million tons, compared to 349 000 tons in Zambia, with CODELCO[163] producing 1.67 million tons of copper, about 41% of Chile's total copper output (CODELCO, 2003:54).

4.4.2 Gross domestic product (GDP) growth

Figure 4.2 shows that the Zambian economy expanded rapidly in the first decade after independence, at an average rate of 6.1% from 1964 to 1974. The unprecedented growth rates that Zambia enjoyed in 1964 (12.9%) and in 1965 (29.4%) were largely attributable to the increasing copper prices. However, the growth rate fell rapidly to an average of 2.6% soon after, in the 1970 to 1974 period. The ten years of relative prosperity (1964-74) were followed by a decline from 1975 to 1980. The high growth rates in the first decade of independence contributed to Zambia's per capita income being the highest in independent sub-Saharan Africa in 1970, at US$420 (World Bank, 1984, cited in Rakner, 2001:530).

[162] Interview with Silane Mwenechanya, 24 October 2003.
[163] Including its production at El Abra, which amounts to 111 058 tons.

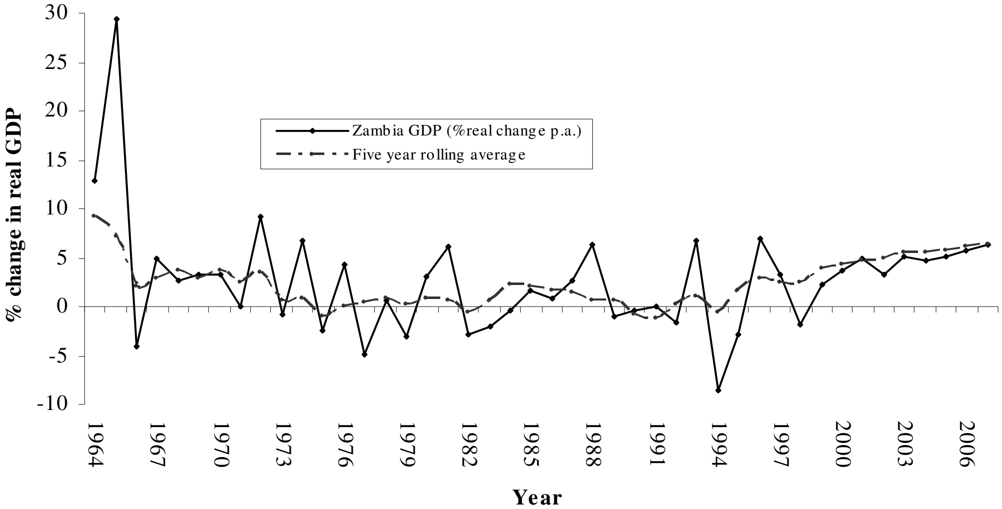
The general declining trend in GDP in the latter part of the 1970s was mainly due to external shocks, principally the collapse of the world copper prices from the mid-1970s and the increases in the price of oil in 1973, forcing the government to resort to foreign borrowing to make up for the growing resource gap (Bank of Zambia, 2003:6; Nalwamba, 2002:20; Cherv, 1989:126, 128, 136; Fraser & Lungu, 2007:54). As a result, Zambia became highly indebted, with substantial debt service costs inhibiting the possibility of economic development in the 1980s. The SAPs of the IMF/World Bank that Zambia adopted from 1983 achieved little or no improvement in GDP growth.

The brief respite in the economic decline in 1988, with the real GDP growth increasing to 6.3%, coincided with the severing of relations with the IFIs in 1987 and the adoption of the NERP from 1987 to 1988. The NERP largely entailed the resumption of greater government control over the Zambian economy (Mwanawina & Mulungushi, 2002:29). The higher GDP growth during the NERP might also have been the result of the greater availability of government resources, enabled through the lowering of its debt services to the IMF and the World Bank to only 10% of net foreign exchange earnings and because of increases in copper prices that broadened its scope to stimulate the economy. However, since the growth enjoyed during the NERP was achieved at a cost of accumulating external debt service, it was unsustainable. Economic growth declined again and remained volatile following the restoration of relations with the IFIs in November 1989.

In the 1990s, which were characterised by rigorous adjustments of the economy, growth in the real GDP was volatile. The GDP fell by an average of 1.15% annually in 1990-95, relegating the Zambian economy to a position as one of the worst performers of African countries not at war, far below the sub-Saharan average of 2-4% (Leistner, 1996:11.13; McGrath & Whiteside, 1989:169; The Economist Intelligence Unit, 2002:34). Again, the collapse in the world copper price and the debt burden were largely to blame, compounded by the negative effects of drought[164] and of flooding on the agricultural sector.

[164] Zambia experienced drought in 1991/1992, 1994-95 and in 1998 in the southern and western parts of the country; flooding also occurred in 1997 and 1998 in the northern parts of the country that damaged the crops.

Figure 4.2: Real GDP growth and average of GDP (at constant 1996 prices from 1980 to 2006)



Sources: IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:12); The Economist Intelligence Unit (2007c, 2008a:13).

Figure 4.2 shows that from 1999 to 2007, Zambia experienced a notable sustained positive GDP growth, averaging 4.57% over this period, for the first time since the late 1960s. The acceleration in the GDP in the early 2000s was partly due to early investments of private mining companies into the Zambian economy (The Economist Intelligence Unit, 2002:28). The increases in the real GDP after 2004, by 5.6% from 2003 to 2007, were mainly as a result of the high global copper prices, which led to fresh investments and increased output in the mining sector (The Economist Intelligence Unit, 2007b:30, 2008b:18). Reductions in debt-servicing costs, through the Highly Indebted Poor Country Initiative (HIPC) initiative for which Zambia qualified in 2005 and particularly because of the Multilateral Debt Relief Initiative (MDRI)[165] that was extended to the country in 2006, were also highly significant in freeing up resources that could encourage economic growth (Fraser & Lungu, 2007:60; The Economist Intelligence Unit, 2007b:43).

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165 The MDRI reduced Zambia's debt to less than 1/10th of the previous level.

4.4.3 Relationships of GDP, mining and manufacturing growth rates

The lack of statistics of growth rates for the same base year as a continuous series makes comparisons of different periods problematic. Figure 4.3 shows that prior to the nationalisation of the mines in 1969 the growth rates in manufacturing did not follow those of mining, mirroring the influences of the practices of mining TNCs to buy input mainly from outside Zambia. Subsequently, the manufacturing sector grew rapidly in particular from 1970 to 1976. From 1972 to 1982 a positive linkage existed for the most part between mining and manufacturing, reflecting the influence of policies of the Kaunda government to develop the local manufacturing sector from mining surpluses. Thereafter, the positive relation broke down with the introduction of SAPs in 1983. The mining sector growth rates were more volatile compared to those of the manufacturing and the agricultural sectors until 1993.

Notwithstanding that manufacturing growth was not consistent it experienced less negative growth than the mining sector before 1994. Moreover, despite the prolonged slump of mining growth for most of the 1980s manufacturing performed relatively well during this period, growing at varying rates. However, the decline in the growth rates of the manufacturing sector in 1985 was mainly because of high increases in the price of imported intermediates (that were unavailable in Zambia) that accompanied the auctioning of the exchange rate in 1985. This led to the erosion of many local industries.

In the 1990s, the year 1994 was marked by a dramatic decline in manufacturing growth mainly because of the liberalisation of trade that culminated into the bankruptcies of many local industries, including backward-linked industries to the mining sector. The liberalisation policies were also highly significant in eroding the relationship between manufacturing and mining growth.[166] In contrast, in 1994 the services sector started to rise considerably. In particular, the financial sector growth rate increased significantly to 113% in 1994 from 3.6% in 1993.[167] The poor relation between mining and

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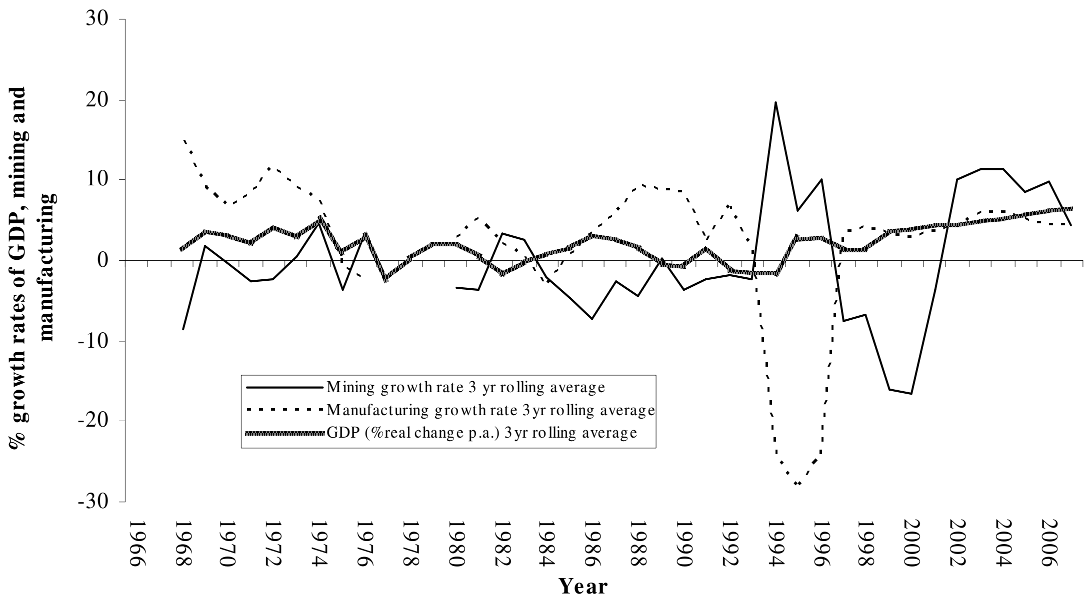
[166] Growth rates in the mining and the manufacturing sectors, however, followed each other in 1992 and in 1996-97.

[167] The tentative calculations based on comparisons of CPI for the base years 1977 and 1994 and the assumption that the 1994 sectoral GDP figures from the CSO are in billions rather than million of kwachas were done to give estimates of 1994 figures in 1977 million kwachas. The calculations provide a rough estimate of the percentage changes in the contribution of the different sectors to GDP from 1993 to 1994 according to the 1977 base year.

manufacturing in 1997 and 1998 was partly as a result of the long delays in the payment of local suppliers to the mines that slowed down manufacturing growth and because of an even greater shift towards the production of consumption rather than capital goods.

Figure 4.3: GDP, mining and manufacturing growth rates* **(rolling averages)**



*The CSO calculated mining and manufacturing growth rates for 1966-70 at constant 1965 prices; 1971-76 at constant 1970 prices; 1978-93 at constant 1977 prices and 1994-2007 at constant 1994 prices. The switch to different base years made calculations of the percentage change from 1976-77 and from 1993-94 not possible. However, the tentative calculations based on comparisons of CPI for the base years 1977 and 1994 and the assumption that the 1994 sectoral GDP figures from the CSO are in billions rather than millions of kwachas[168] were done to give estimates of 1994 figures in 1977 million kwachas. The calculations provide a rough estimate of the percentage changes in the contribution of the different sectors to GDP from 1993-94 according to the 1977 base year.

**2007 value is estimated.

Sources: IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:12); The Economist Intelligence Unit (2007c, 2008a:13); Central Statistical Office (2008).[169]

In the early 2000s, under private ownership of all the mines, the linkage among manufacturing, mining and GDP growth rates was also weaker possibly owing to foreign goods and equipment displacing local manufacturing companies. Despite the poorer linkages manufacturing experienced relatively good growth, from 1.86% in 1998 to 5.7% in 2002 to 7.6% in 2003. However, a closer examination reveals that the growth started from a low base and was mainly as a result of an increase in consumer goods, mostly in the food, beverage and tobacco sector that increased by 81% from 1994 to

168 Most probably a typing error.
169 Statistics were sent on request.

2007. The food, beverage and tobacco sector rose from 59.3% of total manufacturing in 2000 to 65.8% in 2007. Moreover, the textile and leather industry increased considerably from 1994 to 2004 but subsequently declined.

The rather flat rise in the growth trend of manufacturing from the late 1990s and under private ownership of all the major copper mines reflects the decline in the diversity of the manufacturing sector. Moreover, notwithstanding the general increasing trend in the growth of the manufacturing sector under private ownership, the growth rate of manufacturing fell in 2004 to 4.7% from 7.6% in 2003 and in 2005 to 2.9% at the time of high copper prices. At the height of the copper price boom the growth in manufacturing increased to 5.8% in 2006.

4.4.4 Sectoral contribution to GDP

Contribution of mining to GDP

Prior to the nationalisation of the mines mining's contribution to GDP generally decreased from 1965 to 1968, partly because of the increasing contribution of manufacturing to the Zambian economy. Nonetheless, mining sustained a contribution of 30% or more of GDP (49.6% at independence in 1964 and 41% in 1965, compared to agriculture at 13.7% and manufacturing at 6.8% in 1965) until 1974. Subsequently, the shock attributable to the effects of the oil crisis and the decreases in the copper prices, the consequent drop in output and increases in the costs of production from 1974-79 dragged the share of mining to GDP down to about 12% in 1978 and lower until the jump in mining's contribution in 1994.

The relatively low contributions of mining to GDP in the late 1980s and the early 1990s were mainly due to the lower prices and output of copper, the limited foreign exchange that indirectly increased the costs of imported inputs and the subsequent shortage of spare parts for the mining and manufacturing sectors (Cherv, 1989:128; Bank of Zambia, 2003:6). The considerable growth in the manufacturing sector also accounted for the lower contribution of mining to GDP from 1975-89. Higher copper prices and the phenomenal fall in the agricultural and manufacturing sector were chiefly responsible for the increases in the share of mining to GDP in 1994. In the late 1990s, the steep drop in the share of mining to GDP, from 16.7% in 1994 to 6.4% in 2000, was mainly due to the poor reinvestments into the mines from the mid-1990s, the drop in copper and cobalt prices, especially in 1996 and 1998, and the significant reduction in copper mining output (Bank of Zambia, 2003:6).

Under private ownership of the mines the contribution of mining to GDP increased slightly, from the lowest level of 6.4% in 2000 to 7.7% in 2003. This was partly as a result of the impact of fresh investments from private mining TNCs and of increased output in the mining sector (The Economist Intelligence Unit, 2002:34; Fraser & Lungu, 2007:54; Bank of Zambia, 2003:6). The subsequent dramatic increase in the price of copper from 2004 to 2007 resulted in only a marginal increase in the contribution of mining to GDP, to 8.7% in 2006, which was still lower than the 1998 level, when mining's contribution to GDP was 9%. The contribution of mining to GDP dropped in 2007.

Compared to the full range of all the sectors that make up the economy, the share of mining to GDP declined considerably from third to seventh position from 1999 to 2000, corresponding with the period when the privatisation of the last mines was being completed (Mwanawina & Mulungushi, 2002:30). The contribution of the mining sector also dropped below those of agriculture and manufacturing since the late 1990s. It continued to decline under full private ownership of the mines.

<u>Manufacturing</u>

Figure 4.4 shows that the manufacturing sector contributed less to the Zambian economy than the agricultural and mining sectors until 1971. Thereafter, from 1972 until 1992, its share increased significantly resulting in it overtaking the mining sector for the most part from 1977 until 1993. Manufacturing overtook the agricultural sector already in 1971 (except for 1976). The author also relied on statistics from the WDI to show growth trends of the manufacturing and agricultural sector (refer to Figure 4.5) to enable the cross referencing of data provided from the CSO. Although the figures from

the WDI and the CSO do not correspond exactly they display similar trends. The increases in the share of the manufacturing sector to GDP, from only 6.9% in 1965, according to the WDI figures[170] (6.8%, CSO) to 37.1% in 1992 (30.4%, CSO), reflect the positive impact of the concerted industrial policies of the Kaunda government on the development of the manufacturing sector.

However, subsequent to the introduction of strict SAPs during Chiluba's government, the contribution of the manufacturing sector to GDP fell dramatically, from 27.9% in 1993 (26.4%, CSO) to only 11.2% in 1994 (9.8, CSO). Thereafter, it remained at low levels, ranging from 11.2% in 1995 (10%, CSO), 13.4% in 1996 (9.9%, CSO) to 11.1% in 2006 (10.6%, CSO). The steep drop in the manufacturing sector's contribution to GDP in 1994 was mainly attributable to the decline in the dominance of the parastatal sector, following the stricter implementation of more extensive liberalisation programmes during Chiluba's government, which led to the bankruptcies of many locally-based firms in the 1990s (Mwanawina & Mulungushi, 2002:30, 31).

Under private ownership of the mines, the manufacturing contribution to GDP remained low (below agriculture but above mining), ranging from 11.4% in 2000 to 12% in 2003. These levels were lower than the 1998 level of 12.9%. At the height of the copper price boom in 2006 it declined to 11.1%.[171] The manufacturing figures might even be lower, as the heavy weighting of food within the sub-sector, especially maize milling (officially classified as manufacturing), can distort the output figure of the manufacturing sector (The Economist Intelligence Unit, 2008b:15).

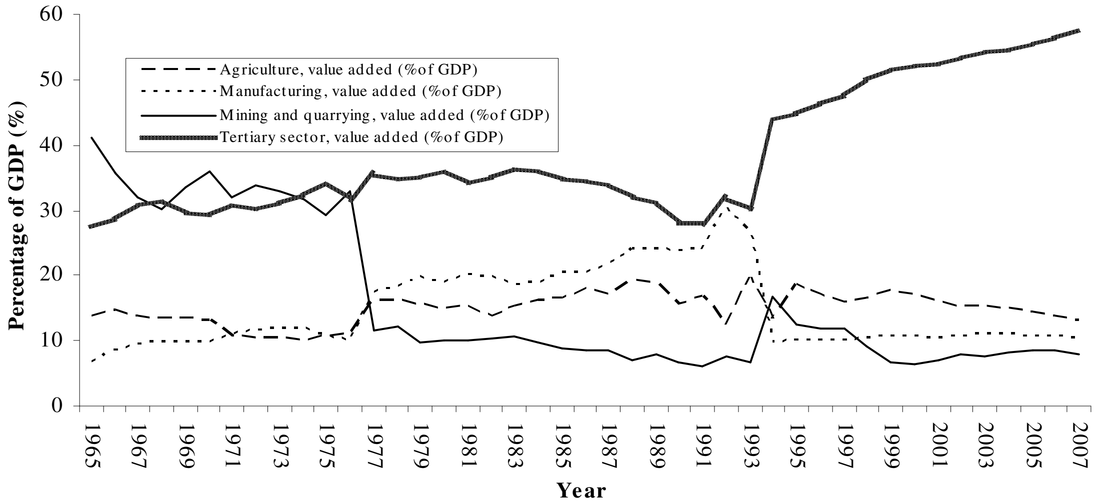
The contribution of other sectors

Growth in agriculture also experienced higher volatility than manufacturing but stagnated in the 1970s till the late 1980s when it reversed. Agriculture became more dominant than mining and manufacturing from 1993/1994. The share of agriculture to GDP was 21.8% in 2006 (13.6%, CSO). However, returns from agriculture are

[170] Based on 2000 constant prices.
[171] The foreign investor friendly policies and other government policies that disadvantaged the domestic producers against foreign producers and the poor socio-economic infrastructure of Zambia, which augmented the transactional costs of local industries, account greatly for the poor performance of local producers (Mwanawina & Mulungushi, 2002:30).

generally poor, with commercial farmers providing almost all the export earnings from the agricultural sector (The Economist Intelligence Unit, 2008b:15).

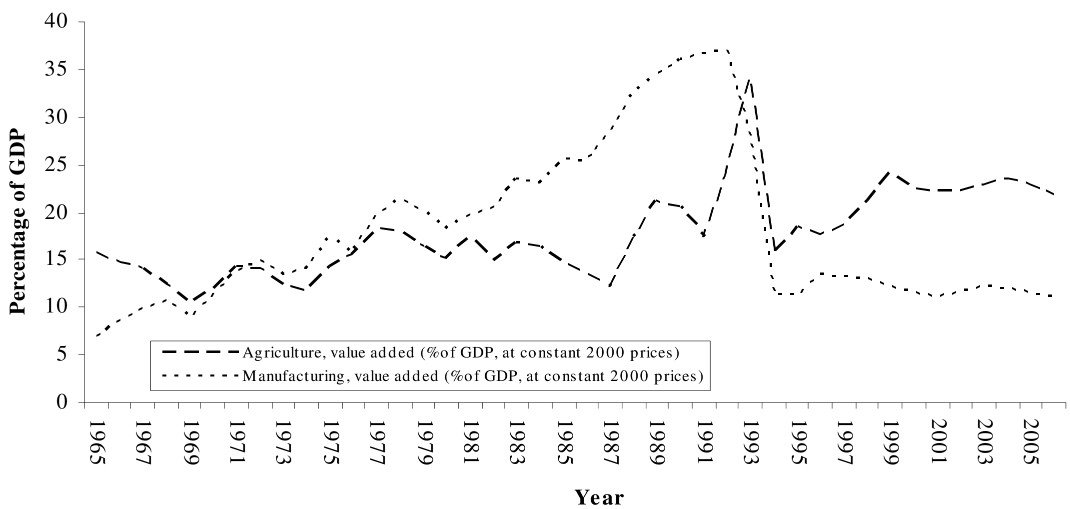
Figure 4.4: Contribution of sectors to GDP



* % of mining to GDP (at constant prices) has been rebased from 1965-69 (using 1965 as the base year), 1970-76 (using 1970 as the base year), from 1977-2007 (using 1977 as the base year).

Source: Central Statistical Office (2008).

Figure 4.5: Contribution of agriculture and manufacturing to GDP

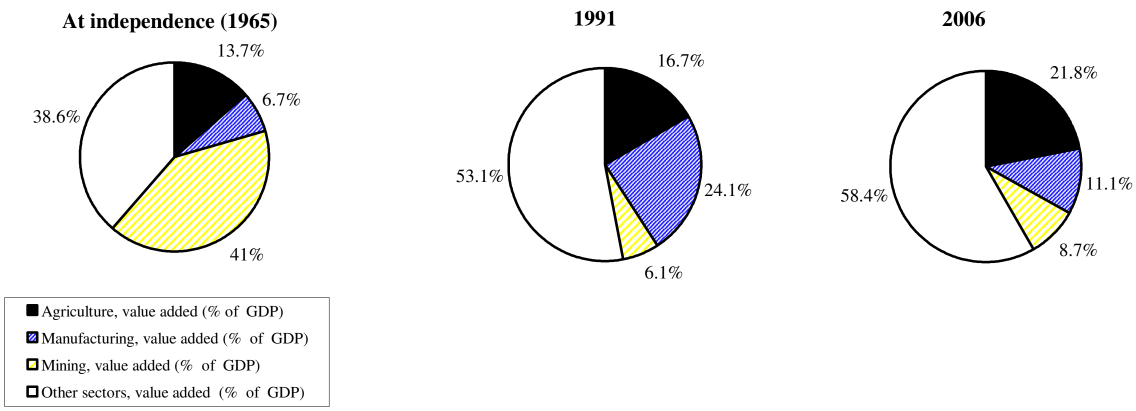


*The % of agriculture and manufacturing to GDP was based at 2000 constant prices. Figures for mining were not available from this source.

Source: World Bank (2009).

While mining and manufacturing declined for most of the 1990s the service sector[172] experienced significant growth. It became the dominant sector from the mid-1990s, as its share increased from 28% in 1991, 30.2% in 1993 to 43.8% in 1994. Figure 4.6 shows the shift in the economy away from manufacturing towards a service nation. The significant change in the structure of the economy especially from 1994 was strongly linked to the introduction of strict SAPs (The Economist Intelligence Unit, 2008a:6, 2008b:20; Mwanawina & Mulungushi, 2002:30).

Figure 4.6: Shifts in sectoral contributions to GDP in the Zambian economy



Sources: Central Statistical Office (2008).[173]

The service sector continued to grow under private ownership of the mines to 57.5% in 2007.[174] Accordingly, it became an important driver of economic growth (The Economist Intelligence Unit, 2002:28, 2008b:20). Since the official statistics for the service sector capture an unknown proportion of total activity they should be treated with caution (The Economist Intelligence Unit, 2002:28). Figure 4.6 shows that the agricultural sector's contribution to GDP also increased notably from 1991 to 2006.

[172] Made up of the electricity, gas and water; construction; restaurants, bars and hotels; transport, storage and communications; financial intermediaries and insurance; real estate sectors.

[173] Author's own calculations done from information sent by CSO on request.

[174] The largest sub-sectors within the services sector in 2003 and in 2007 were the wholesale and retail sector followed by the real estate and business services. The financial intermediaries and insurance sub-sectors were the third most important sector in 2003 and ranked fifth in 2007 after the transport storage and communications sector (mainly because of increasing share of cell phone companies) and the government services. Growth would likely continue in the communications and tourism sectors.

4.4.5 Human Development Index and poverty levels of Zambia

The Human Development Index (HDI[175] – measuring the average progress of the human development of a country) of Zambia dropped below the average of sub-Saharan Africa from 1991 and remained below this level until 2007, when it was last recorded. While the HDI has increased progressively in almost all regions from the mid-1970s, it stagnated in sub-Saharan Africa since 1990. The stagnation was partly because of economic reversals and because of the catastrophic effects of HIV/AIDS on life expectancy (UNDP, 2007/2008).

Also, the rise in Zambia's HDI between 1980 and 1985 under Kaunda's rule was reversed at an increasing rate, from 1987.[176] Zambia, in fact, became the only country in East, Central and Southern Africa to experience a worsening in its HDI[177] by 1997, from the 1975 level. Zambia's HDI dropped by 5.4% between 1990 and 1997 and reached its lowest level in 2000, after which it increased only marginally (UNDP, 2001:35-36, 2009). Between 1990 and 2007, Zambia's HDI fell by -0.17% annually from 0.495 to 0.481, ranking it 164th out of 182 countries in 2007. In 2005, the HDI of Zambia was 0.434 (UNDP, 2007/2008, 2009).

Moreover, in 2005, Zambia's Human Poverty Index (HPI-1), focusing on the most deprived in multiple dimensions of poverty, or the proportion of people below a threshold level in the same dimensions of human development as measured in the HDI,[178] was 41.8. This ranked the country 96th among the 108 developing countries for which the index has been calculated (UNDP, 2007/2008). The introduction of excessively liberal policies under MMD rule, from the 1990s, especially in the real sectors of Zambia, alongside the removal of subsidies (an important requirement of SAPs) compounded the poverty levels of Zambia.

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175 Which represents a better measure of poverty than income.

176 The HDI, however, also dropped but at a lower average rate of 4.4% between 1985 and 1990, which corresponds to a time of IMF and World Bank involvement in Zambia (UNDP, 2001:35-36).

177 Account nevertheless needs to be taken of the fact that since life expectancy forms part of the HDI, the lower HDI is partly influenced by the higher incidence of AIDS in recent years in Zambia.

178 Living a long and healthy life, having access to education and a decent standard of living.

Official poverty figures[179] show that poverty reached unprecedented levels in Zambia, rising from 69.7% in 1991 to 73% in 1998.[180] The poverty levels are significantly higher if basic needs such as shelter, education, healthcare, lighting, clothing, footwear and transport are taken into account (Mwanawina & Mulungushi, 2002:31). The negative trends in human development that accompany SAPs and neo-liberal policies, imposed by the World Bank and the IMF, suggest that additional measures are needed to minimise the erosion of human development in the process of reforming the economy through macro-economic stability (UNDP, 2001:39).

4.4.6 Total employment and mining employment in Zambia

Total employment grew faster than mining employment from 1979, indicating a diversification in sectors other than mining from this date. During 1985-91, total employment and mining employment were stable and were sustained at high levels, but began declining sharply between 1993 and 2003, with the decrease in mining employment being more significant. The mining sector's share of total formal sector employment dropped from 22.2% in 1963 to 15.9% in 1984, 11.9% in 1990 and to 7.3% in 2000 (Fraser & Lungu, 2007:3). The discussion below elaborates on the total and mining employment of Zambia.

<u>Total employment</u>

Total formal employment of Zambia increased steadily from independence in 1964 at 268 700, to a peak of 546 000 in 1992 (Figure 4.7). Subsequently, about 80 000 formal sector jobs were lost from 1992 to 1998. The drop coincided with the institution of more rigorous SAPs, liberalisation and privatisation policies since the 1990s.

At present, the overwhelming majority of the labour force of Zambia is employed in the informal sector,[181] whose share of total employment has grown considerably from the

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179 Based on the percentage of the population below the established poverty line, determined through a food basket of minimal caloric requirements of a predominantly vegetarian list of food.

180 Poverty levels might even be higher than the official figures, possibly 98%, if non-vegetarian food and basic needs, such as shelter, education, healthcare, lighting, clothing, footwear and transport were included in the food basket (CSO, 1998, cited in Mwanawina & Mulungushi, 2002:31).

181 Dominated by women.

early 1990s (Tshoaedi, 2000:87; World Bank, 2002b:18). Formal sector employment[182] that accounted for merely 19.1% of the total labour force in 1990 dropped further to only 10.6% in 2000. Informal sector employment increased from 68.9% in 1990 to 76.4% in 2000, and was 73.9% in 2005. Official unemployment levels were 12% in 1990, which increased to 20% in 1993 and were 16% in 2005. However, unofficial sources cite much higher unemployment rates for Zambia under MMD rule. This is because many people regarded as employed in the informal sector in official figures, are considered as unemployed in unofficial sources. Accordingly, a staggering 3.39 million or 89.4% of workers were either unemployed or employed in the informal sector in 2000 (The Economist Intelligence Unit, 2007c; Central Statistical Office, 2006; World Bank, 2009; Regional Investor Survey, 2001:44; Catholic Secretariat, 2001:12; Ministry of Finance and National Planning, 2002b:74).[183]

Most retrenchments (approximately 54 000) occurred in the 1990s before privatisation policies were introduced. The lower employment levels in the 1990s were mainly owing to the bankruptcies of several industries as a result of increased competition emanating from trade liberalisation and the removal of controls, rather than the privatisation process,[184] according to the Zambia Privatisation Agency (ZPA)[185] (2000a:20; 2000b:16).

<u>Mining sector employment</u>

Figure 4.7 shows that mining employment increased, especially in the 1960s and the 1970s, from 57 130 in 1963 to a peak of 81 311 in 1975.[186] Subsequent to the introduction of SAPs, mining employment fell considerably to only 64 500 in 1985, shifting it from first position over 1960-84 to third position between 1985 and 2006,

[182] The public sector, namely, the central and local government and the parastatals, is the largest formal sector employer in Zambia (The Economist Intelligence Unit, 2008b:21).
[183] The figure was 81.3% in 1991.
[184] The ZPA ascribes the loss in employment in the non-mining sector due to privatisation at only 6 000 out of a total of 60 000 formal sector job losses between 1992 and 1996. Moreover, out of the 6 000 that were retrenched, 4 000 were on account of the collapse of the state trade sector prior to privatisation (ZPA, 2000a:20).
[185] Interview with Stuart Cruickshank, Advisor of ZPA, 28 October 2003.
[186] After agriculture, manufacturing was the second largest employer in the formal sector with an estimated workforce of 68 000 in 1994.

after agricultural and manufacturing employment.[187] Despite the considerable drop from the 1976 levels, mining employment was still relatively high in 1991 at 64 800.

Figure 4.7: Total and sectoral employment in Zambia

*Note: mining employment figures from the Association of Copper Mining show a less significant decline in the 1980s than the CSO figures.

Sources: Central Statistical Office, Quarterly Employment and Earnings Inquiry and the Monthly Digest of Statistics (2006); The Economist Intelligence Unit (2006:61).

Subsequently, before the mines were even privatised, huge reductions took place in the mining sector workforce in the 1990s. About 19 600 employees lost their jobs at the ZCCM from 1992-97, with the workforce dropping to only 42 498 in 1997, when the first mines were privatised. The decline in the workforce before the mines were privatised was mainly as a result of the cost-cutting measures of the Chiluba government in the 1990s.[188] These measures were rooted in fiscal pressure and the SAPs of the IMF and the World Bank, demanding significant reductions in government expenditure, including the streamlining of the workforce of the ZCCM.[189] Demands from these bodies after 1993 that the government curb the expansion of government investments into enterprises in line for privatisation, beyond maintaining their physical

[187] Employment figures from the Association of Copper Mining Employers, though, show a less significant decline in employment levels in the 1980s, than those of the CSO.
[188] Interviews with Stuart Cruickshank, 28 October 2003 and Francis Kaunda, 20 October 2003.
[189] Interview with Charles Muchimba, 18 November 2003.

assets intact, also reduced employment opportunities in the mining sector in the 1990s (Andersson, 2000:75).

Under private ownership of the mines, many permanent mineworkers further lost their jobs in the short term. This is mirrored in the steep fall in permanent employment from 38 521 in 1999 to only 22 000 in 2000 and to its lowest level of about 19 000 in 2002. The permanent mining employees dropped in 2002 by 19 521 or 50.6% of the level reached in 1999 (Fraser & Lungu, 2007:3, 21, 22; Van Buren, 2003:1151; World Bank, 2002b:4, 18). This was mainly as a result of the tendencies of mining TNCs to increasingly shift workers into fixed-term employment and more important, into subcontracting work, through external contracts, elaborated upon in Chapter 5.[190] The variations in the types of contracts offered under private ownership of the mines render it difficult to calculate the exact number of people working in the industry under different terms and conditions since the mines were privatised (Fraser & Lungu, 2007:22). If fixed-term and subcontracting employment are taken into account then the total mining employment amounted to 35 042 in 2000.

The copper price boom in 2005 and 2006 contributed to the increases in the total permanent and non-permanent employment figures in the mines to 38 700 by September 2006, in the five firms that make up the biggest share of mining employment. The increases were, though, mainly in indirect employment, through contract and fixed-term employment, which together comprised then 46% of mining employment in 2006. Permanent employment levels increased only slightly to 21 000 in 2006 (Fraser & Lungu, 2007:22). Although copper mining is the main contributor to export earnings, it is no longer labour-intensive and dropped below agricultural and manufacturing employment already since 1985. Currently it accounts for a relatively small proportion of formal sector employment (The Economist Intelligence Unit, 2008b:21).

As far as the relations among employment in mining, agriculture and manufacturing are

[190] Interview with Charles Muchimba, 18 November 2003.

concerned, Figure 4.7 shows that from 1970 to 1984, except for the 1976 to 1979 period, employment levels in all the sectors generally increased. Subsequent to the fall in mining employment from 1984 to 1985 the agricultural sector, which was in third position, overtook the mining and manufacturing sectors (apart from 2002) as the dominant employer from 1985 until 2003. Manufacturing employment remained reasonably stable from 1985 until 1991, and then dropped considerably together with mining employment from 1993 to 2001, coinciding with the time that excessive SAPs and liberalisation and privatisation policies were introduced in the Zambian economy. Manufacturing employment nevertheless remained above the levels in mining from 1985 to 2002.

4.4.7 Mining's contribution to exports

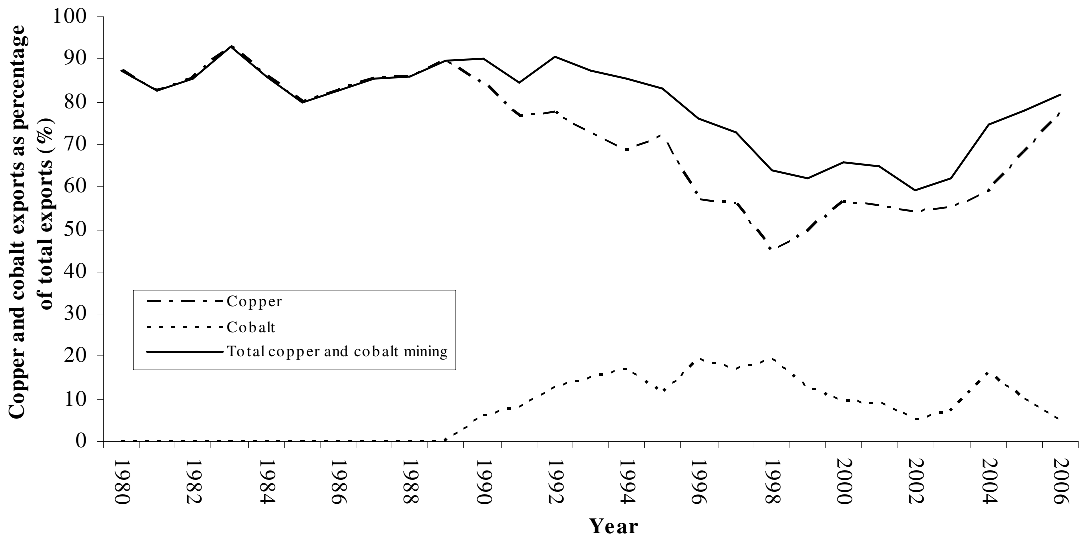
Copper mining contributed 96.5% to total mining output in 1987 and copper and cobalt[191] (a by-product of copper) production still accounted for 90% of mining production in 2006, rendering copper mining highly representative of the mining industry in Zambia (Saasa, 1987:7; The Economist Intelligence Unit, 2007b:25, 34). Moreover, the mining sector is the most important contributor to the foreign exchange earnings of the Zambian economy,[192] boasting for the most part over 90% of Zambia's export earnings[193] since independence (The Economist Intelligence Unit, 2002:39; World Bank, 2002a:4; Maambo, 1998:Fig. 7). Mining exports contributed 99% to total exports in 1970 and copper and cobalt mining still accounted for 90.4% of Zambia's foreign exchange earnings in 1992.

However, Figure 4.8 shows that from 1994 to 2002 a considerable decline took place in the share of copper and cobalt exports to total export earnings, from around 85.3% in 1994 to its lowest level of only 59.3% in 2002. The progressive drop in the export earnings from copper during this time were largely attributable to the periodic slumps of the international copper price, the fall in production levels (in 2000 below a third of its peak) and to increased production costs, mainly owing to a lack of reinvestment in the

[191] That acquired importance only in the mid-1980s.
[192] Interviews with Silane Mwenechanya, 24 October 2003 and Wilphred Katoto, 12 November 2003.
[193] Interviews with Dennis Wood, 21 October 2003; Silane Mwenechanya, 24 October 2003 and Wilphred Katoto, 12 November 2003.

mines (Catholic Secretariat, 2001:12; Van Buren, 2003:1151; Leistner, 1996:11.19; Akwetey, 1994:53). The major disruptions in mining activities that accompanied the privatisation process further accounted significantly for the decline in copper earnings (Committee on Economic Affairs, 2000:60 and 110). The increase in the production of cobalt in the 1990s, from 6.2% of export earnings in 1990 to 19.2% in 1998, cushioned the mining sector somewhat against a bigger drop in its contribution to exports.[194]

Figure 4.8: The contribution of mining to total exports



Source: The Economist Intelligence Unit (2007c).

From 2004, the share of copper and cobalt mining to total export earnings rose notably to 74.6% and increased further to an estimated 81.9% of goods exported in 2006, coinciding with surging international copper prices. Consequently, the mining sector grew by almost 50% in real terms from 2001 to 2005 (The Economist Intelligence Unit, 2007b:25, 34). While mining will continue to be a major economic activity in Zambia, its contribution to export revenue is however likely to remain below its pre-1991 levels.

The fall in export earnings in the decade between 1992 and 2001 had a devastating impact on Zambia's balance of payments, investments, exchange rates and the foreign exchange reserves. The poor balance of payments exacerbated the country's

[194] The drop in the share of cobalt to export earnings in the early 2000s, under private ownership of the mines, from the 1998 level was mainly as result of the depletion of cobalt resources at KCM and the non-production at Roan Antelope Mining Corporation of Zambia (RAMCOZ) (Ministry of Finance and National Planning, 2002a:62).

indebtedness. Moreover, under private ownership of the mines an increase in export earnings did not necessarily translate into considerable benefits for Zambia, since most of the income was repatriated out of the country that also had a negative influence on the income debit of Zambia. The impact of the changes in the export earnings on these economic variables and of the repatriation of mining surpluses on the income debit of Zambia are examined below.

4.4.8 Balance of payments

The mining sector's[195] domination of Zambia's foreign exchange renders the balance of payments position of the country highly dependent on the performance of mining. Accordingly, the same external factors that contribute to a decline in the performance of the mining sector have a negative impact on the trade balance of Zambia. These factors include a drop in the production and price of copper and, more recently, of cobalt, driven largely by the international demand for these metals and increases in the price of oil, a major input in mining (The Economist Intelligence Unit, 2002:40, 2007b:41; World Bank, 1996:4; Cherv, 1989:129; Seidman, 1977:236).

Throughout the 1960s, until 1974, Zambia experienced a balance of payments surplus, averaging 1.4% of GDP per annum, mainly owing to the high world copper prices. However, the surpluses declined consistently from 1974. The interaction of higher oil prices and the world economic recession that caused a drop in the price of copper, as well as increases in both visible and invisible imports, accounted for Zambia's high balance of payments deficits from the mid-1970s (World Bank, 1996:4; Cherv, 1989:129; Seidman, 1977:236). The balance of payments difficulties that Zambia experienced in the mid-1980s were mainly as a result of the widening gap between the debt servicing and payment capacity of the government and the dramatic rise in the costs of imports, following the auctioning of the exchange rate in 1985 (McGrath & Whiteside, 1989:180).

Figure 4.9 shows that Zambia experienced trade deficits for most of the 1990s. The

[195] Especially copper and cobalt mining.

trade deficits increased even more, in the short term, under private ownership of the major copper mines. The deficits were significantly influenced by the slower decline in imports,[196] relative to the decrease in the share of exports to GDP[197] or by the increases in imports that, for the most part, far outweighed exports. Zambia was, therefore, a net importer of goods and services at the time.

The introduction of strict trade liberalisation in 1995 facilitated the huge imports of goods and services. The devaluation of the kwacha following the auctioning of the exchange rate in 1994, which dramatically increased the costs of foreign goods for the highly import-dependent economy and the declines in the production of copper also accounted greatly for the trade deficits in the 1990s. However, the country enjoyed trade surpluses in 1991 (at US$42 million), 1994 (at US$64 million) and in 1997 (at US$54 million), coinciding either with higher copper prices (1991 and 1994) or rising levels of copper production (1997) in Zambia (World Bank, 1996:4; The Economist Intelligence Unit, 2002:47, 2007b:41).

Zambia experienced its highest trade deficits in the first few years under private ownership of the mines. The trade deficit peaked at US$341 million in 2001, the highest level on record, and was still high in 2003 at US$312 million. The increasing trade deficits that Zambia experienced under private ownership of the mines in the short term between 1998 and 2003, were mainly owing to the surge in imports,[198] alongside the decline in exports. In 2003 imports, spurred on by greater investments in mining (which have a substantial import component) as a result of the higher copper prices, climbed to US$1 393 million, concurrently with declining exports (Africa Analysis, 2003b:20; Ministry of Finance and National Planning, 2003:28; The Economist Intelligence Unit, 2007b:41).

A lower balance of payments support than what was pledged by multilateral donors, together with the sharp rise in global petroleum oil prices, a major component of the

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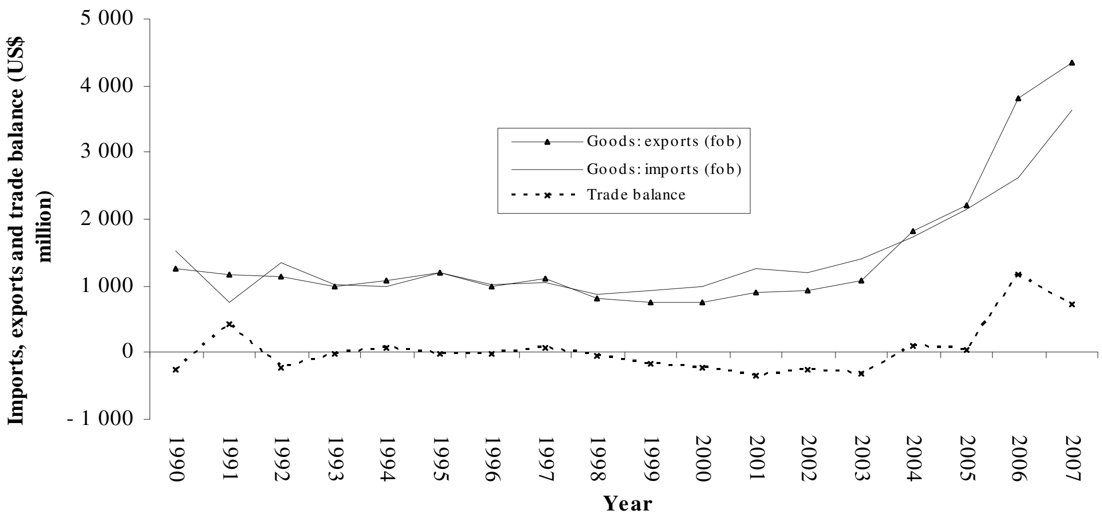
196 From 39% of GDP, between 1965 and 1974, to 34%, between 1990 and 1995.
197 From about 50% to about 31%, during the respective periods that contributed to the bankruptcy of many locally-based mining companies.
198 By 6% in 2000 and 28% (20.2% of GDP) in 2001.

import bill,[199] hindered further improvements in the balance of payments position of Zambia at the start of the 2000s. Capital equipment, a major input component to the mines, and consumer goods account for most of the remainder of the import bill (The Economist Intelligence Unit, 2008b:23; Africa Research Bulletin, 2001b:14647). Substantial increases in food imports[200] also contributed to the greater trade deficit in 2002 (Government of Zambia, 2002: paragraph 19). The high trade deficit constituted a major macroeconomic challenge for the country (Africa Research Bulletin, 2001b:14647; The Economist Intelligence Unit, 2002:47).

Figure 4.9: Imports, exports and trade balance



Sources: The Economist Intelligence Unit (2007c, 2008a:13).

However, Zambia enjoyed trade surpluses from 2004-07. The trade surpluses increased dramatically from about US$35 million in 2005 to a peak of US$1 183 million in 2006, despite the rise in imports by an annual average of around 20% from 2003 to 2006 (The Economist Intelligence Unit, 2007b:41). Huge increases in copper exports,[201] around four times the level recorded in 2002[202] that outweighed surging imports, which led to a fall in the drag that net trade imposed on the GDP, accounted mainly for the higher trade surpluses (The Economist Intelligence Unit, 2007b:41, 2008b:15, 23). Total

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[199] Owing to repeated supply disruptions from the Indeni refinery in Ndola that necessitated the import of refined petroleum products, rather than crude oil.
[200] Mirrored in the 6.8% increase in merchandise imports during the second half of 2002.
[201] To an estimated US$3.1 billion in 2006.
[202] Due to the boom in the prices of copper and, to some extent, because of the benefits accruing from the greater investments in the copper mining sector.

exports in general increased in value to US$3.8 billion in 2006 (with growing domestic production), that is, by 73% from the 2005 level. Subsequently, in 2007, the trade surplus dropped to US$726 million, chiefly as a consequence of the significant rise in imports from 2006 to 2007 (The Economist Intelligence Unit, 2007a:6).

4.4.9 Income debit

A study of the income debit, encompassing payments abroad,[203] including the debt interest payments of the country, profits and dividends, plus all forms of employee compensation, provides a good indication of the outflows of revenue from Zambia due to the repatriation of profits and dividends from mining TNCs and of employee compensation. Before 2004, the external debt service or interest payments on external debt have been the main income debit component in Zambia. However, more recently, the huge debt relief granted to Zambia in 2005 and 2006 reduced the influence of debt service on the income debit of Zambia.

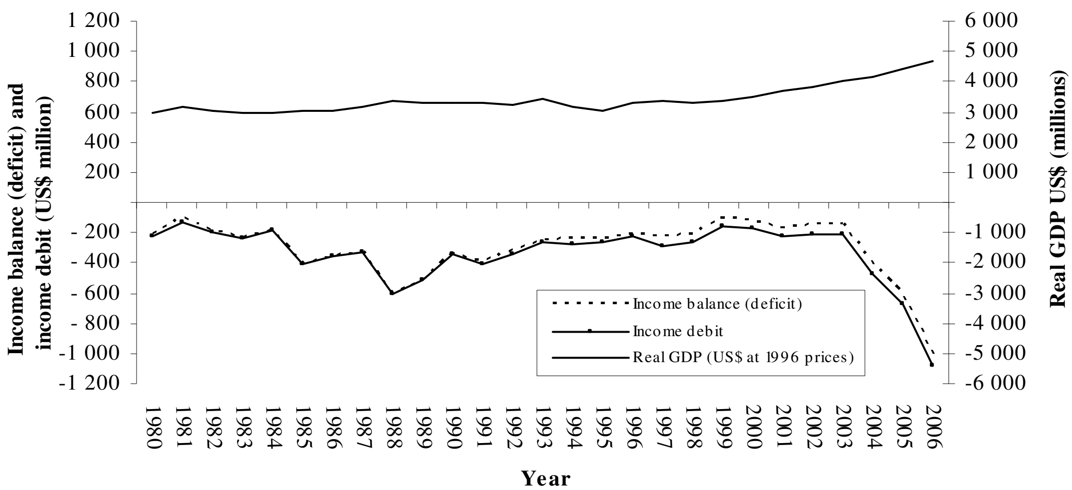
Figure 4.10 shows that, except for the years 1988-89 and 2004-06 and to a lesser extent, 1985 and 1991, the income debit of Zambia remained rather small, ranging from US$130 million in 1981 to US$354 million in 1986. The substantial increase in the income debit of Zambia to US$604 million in 1988 from the 1981-86 levels was possibly due to the accumulation of high debt servicing as a result of the NERP that the Kaunda government adopted. At the time the government limited its debt service payments owed to multilateral institutions.

In spite of the dramatic improvements in the performance of the mining sector from 2003 to 2006 and the increases in GDP, the income debit and income deficit of Zambia rose enormously during that time. The income debit increased to unprecedented levels in 2006, of US$1 075 million, for the period covering 1980 and 2006. The dramatic increase in the income debit was chiefly as a result of large repatriations of profits and shareholder dividends of foreign-owned mining companies and of remittances or compensation of foreign employees out of Zambia, under the foreign private ownership

[203] In respect of foreign-owned investments in the domestic economy.

of most of the companies in Zambia. This is to some extent supported by the fact that the external debt service or interest payments on external debt, previously the main income debit component of Zambia, declined enormously[204] since 2005 and particularly in 2006, from US$729 million in 2003 to only US$174 million in 2006 (The Economist Intelligence Unit, 2008a:7, 2008b:24). Accordingly, a huge component of gains from the increased GDP did not benefit the Zambian economy, as large sums of mining profits were repatriated out of the country specifically at the time the mining sector gained significantly from the high copper prices.

Figure 4.10: Real GDP, income debit and income balance (deficit)



Source: The Economist Intelligence Unit (2007c).

4.4.10 Inward direct investment (net direct investment flows) and capital investment

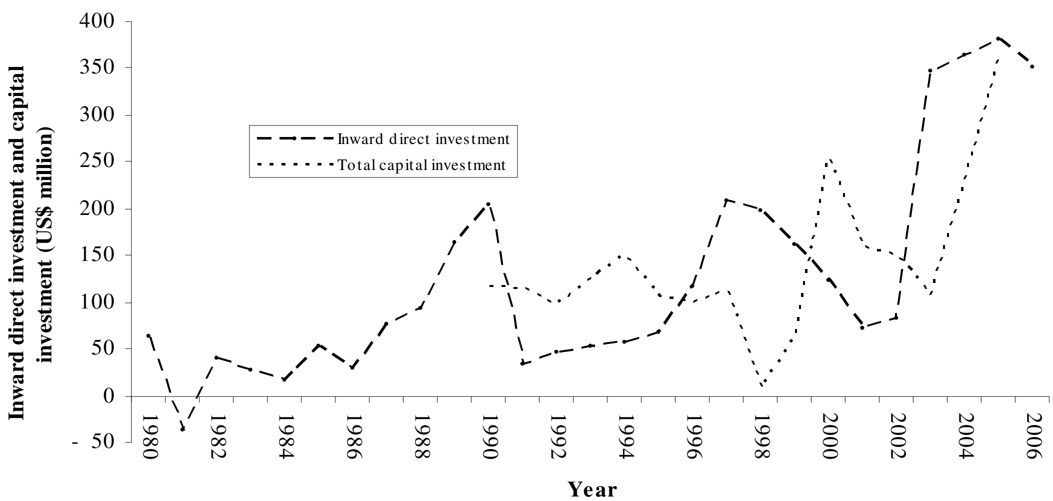
Figure 4.11 shows that the inward direct investment (or the net direct investment flows of capital by non-residents into the country) into Zambia was highly unstable, especially from 1989 to 2006. The inward direct investment flows were low from 1980-88. There was a net outflow of direct investment in 1981. The investment flows were relatively high in 1990 and in 1997-98 and increased considerably from 2003-06.

The substantial increases in the inward direct investment flows in 1990 to US$203 million from US$93 million in 1988 were possibly encouraged by the market-

[204] Principally as a result of the enormous debt-reduction and debt forgiveness that Zambia secured with creditors.

oriented policies that the Kaunda government adopted, specified in the PFP covering the 1989-93 period. However, from 1991 to 1995 the inward direct investment of the private sector dropped sharply to only US$34 million in 1991 and remained at low levels till 1995. The annual average net flow of direct investment from 1991-95 was only US$50.8 million, compared to the average of US$133.7 million in the late 1980s, during 1987-90. The low foreign investment during 1991-95 coincided with the uncertainty created during the 1991 elections and the transformation period before the privatisation of the non-mining economy and of the mines. Moreover, several foreign companies relocated from Zambia, following huge inflows of cheaper foreign inputs into the country as a result of trade liberalisation policies (discussed in Section 4.2.2.1 above).

Figure 4.11: Inward direct investment and capital investment



Sources: The Economist Intelligence Unit (2007c); Chamber of Mines, 2006 (cited in Fraser & Lungu, 2007:77).

The higher levels of net direct investment in 1997 to US$207 million and in 1998 at US$198 million from US$67 million in 1995 reflect the impact of the ambitious privatisation programme, in particular the sale of Zambia Sugar in 1998 to Tate and Lyle and the Commonwealth Development Corporation (CDC) for US$70 million (Ndulo, 1999, cited in Andersson, 2000:77). However, despite the privatisation of the mines that started in 1997 and was completed in 2000, the net direct investment levels declined sharply between 1999 and 2001, from levels obtained in 1998, dropping to

US$72 million in 2001. These levels were also low in 2002.

The low net direct investment, in the short term, from 2000-2002, under private ownership of all the major copper mines, possibly reflects an initial wait-and-see attitude of private investors. This coincides with the ‘real options view of investment’. This view is based on the assumption of irreversible investment costs (namely, the capital loss to the investor when disposing of investment goods in a second-hand market), and on the uncertainty of future pay-offs and of future output prices that encourage investors to postpone their investments (Dixit and Pindyck, 1994, cited in Andersson, 2000:79). The larger the uncertainty and the higher the value of the potential investment, the greater would be the likelihood that the firm would postpone the investment decision (Andersson, 2000:79). Possible investments that foreign companies possess elsewhere would likely lessen losses in returns that they might incur from the postponements. These arguments are also considered in Section 6.1.2 of Chapter 6.

However, the subsequent sharp rise in the net direct investment between 2003 and 2006 under private ownership of the mines was largely thanks to the dramatic increases in the prices of copper at the time that encouraged higher investments in the mining sector. The net investment flows reached their highest level in 2005 at US$380 million, for the period covering 1980 to 2006. The investment levels rose further from US$82 million in 2002 to US$364 million in 2004. However, these levels dropped slightly to US$350 million in 2006.

Figure 4.11 shows that capital investment also proved rather unstable in the short term under private ownership of the mines. The considerable volatility reflects the significant influence of the price of copper on capital investment under private ownership and possibly a reluctance of mining TNCs in the short run not to respect their investment obligations. The capital investment dropped enormously in 1998 to only about US$8 million, from about US$116 million in 1997. Subsequently, it increased steadily until 2000, reaching about US$252 million, but declined again from 2001-2003 to around US$112 million in 2003. In the years of high copper prices capital investment increased steeply from 2004 to 2005, reaching about US$352 million in 2005.

4.4.11 Exchange rates

The significant contribution of the mining sector to Zambia's foreign exchange and the vulnerability of copper mining to external factors render the kwacha highly susceptible to the performance of mining and indirectly to the influences also of external factors. The external factors that influence the exchange rate encompass the world demand for copper products, the prices of copper and the performance of the US dollar.[205] Moreover, aid and debt forgiveness were becoming increasingly important in supporting Zambia's foreign exchange earnings that indirectly influence the exchange rate.

Internal factors that affect the local exchange rate include increases in the imports of mining inputs and a rise in the costs of the production of copper (Nalwamba, 2002:5). Additionally, under private ownership of the mines and in the absence of greater exports in other sectors, the ability of private mining companies[206] to remit profits from mining sales out of Zambia could also affect significant reductions in the foreign exchange levels. This would, in turn, cause a depreciation of the kwacha. Rather than encouraging local entrepreneurship, the poor capacities of local industries precluded them from taking advantage of incentives that a depreciation holds for building local entrepreneurship, discussed above.

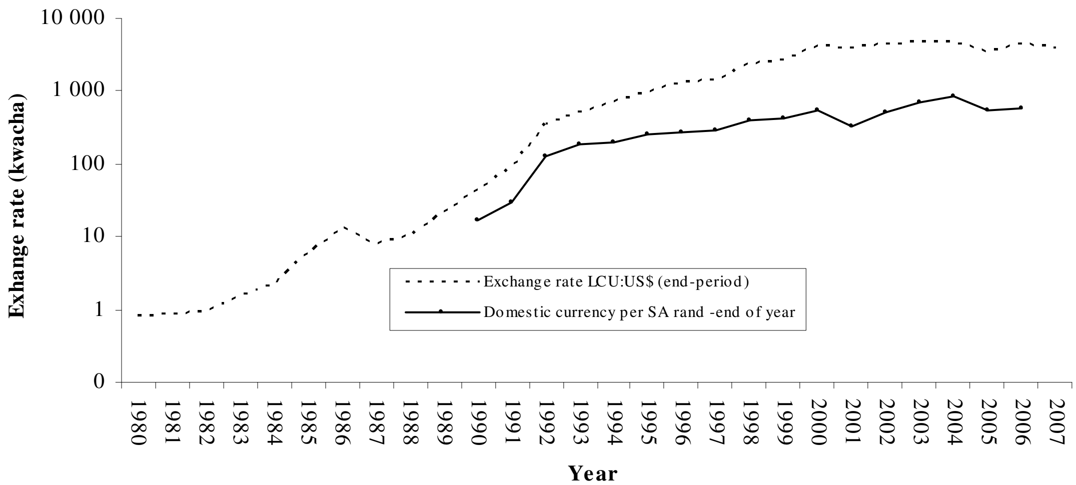
In the 1980s, the introduction of the auctioning of the foreign exchange system in 1985 resulted in a depreciation of the kwacha. Before this, the stringent allocation system under the controlled foreign exchange regime, the Foreign Exchange Mechanism Allocation System (FEMAC) contained significant declines in the value of the kwacha. The kwacha fell from US$1=ZK0.8 in 1980 to US$1=ZK21.7 in 1989 (Maambo, 1998:Figs. 7, 8). The control that the NERP reintroduced in the foreign exchange market from 1987-88 accounted for the brief increase in the value of the kwacha in 1987 to US$1=ZK8 from US$1=ZK12.7 in 1986. Severe shortages of foreign exchange, largely due to the IMF and the World Bank and other bilateral bodies failing to provide

[205] The currency in which the price of copper and cobalt is quoted.
[206] Because of the lack of exchange controls.

funding to Zambia, as retribution for the government's introduction of the NERP policies in 1987-88, led to the fall in the kwacha after the NERP during Kaunda's government.

Figure 4.12 shows that a more dramatic depreciation in the value of the kwacha took place against both the US dollar and the rand, the currencies employed by Zambia's main trading partners during the 1990s since the beginning of Chiluba's rule, and especially under private ownership of the mines. The decline in the kwacha was much more pronounced against the US dollar. The enormous depreciation and volatility of the kwacha against the US dollar and the rand from 1994[207] coincided with the auctioning of the exchange rate that opened the economy to external shocks.[208]

Figure 4.12: Kwacha exchange rate with US dollar and rand (represented as a log graph)



Sources: The Economist Intelligence Unit (2007c, 2008a:13); Bank of Zambia (2000).

Within less than a decade, from the beginning of Chiluba's rule in the early 1990s till 1999, the kwacha declined, sharply, from US$1=ZK88.97 in 1991 to US$1=ZK2 632.2

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207 Despite occasional efforts by the BoZ to support the exchange rate. While the BoZ has no formal powers to set the exchange rate, it periodically intervenes in the market, through currency purchases and the manipulation of statutory reserve ratios, to influence the value of the kwacha. Moreover, while intervention by the central bank might smooth out short-term fluctuations, this would postpone rather than avert a sharp depreciation (which was historically the case), especially as foreign exchange reserves are expected to increase slowly, to around only three months of import cover (The Economist Intelligence Unit, 2007a:6, 2007b:28).

208 A fully liberalised or market-determined exchange rate commenced in 1994 (following the opening of the Open Central License in February 1990, the floating of the kwacha in October 1992 and the inter-bank foreign exchange system in December 1993). Trade in foreign exchange was further liberalised in July 2003, through the elimination of the requirement of clearance, also of major foreign-exchange transactions, through the BoZ's dealing window (The Economist Intelligence Unit, 2007b, 2007c:44; World Bank, 2002a:14).

in 1999, representing a depreciation in the nominal exchange rate of 2 858%. The kwacha depreciated against the rand from R1=ZK30 in 1991 to R1=ZK549.7 in 2000. The considerable depreciation of the kwacha against the US dollar in the late 1990s was mainly owing to the withholding of balance of payment support and the significant reductions in export earnings, because of a weaker performance of the mines and the decline in the price of copper in 1998, following the East Asian crisis of 1997 (SADC, 2000:340).

Under private ownership of all the copper mines, increased investments and higher inflows of balance of payments support from donors did not result in an improvement in the value of the kwacha against the US dollar until 2004. On the contrary, the kwacha depreciated dramatically against the US dollar to US$1=ZK4 157.8 in 2000 from the 1999 level of US$1=ZK2 632.2 and plunged to its lowest level in 2004, at US$1=ZK4 771.3, amounting to a decline of 81% from 1999 to 2004. The kwacha also displayed high volatility, against both the rand and the US dollar exchange rates, especially from 1999 to 2004.

Subsequent to the huge savings as a result of the debt relief and other donor support[209] granted to Zambia, the strong copper exports following unprecedented high prices and a growing investor confidence,[210] the kwacha appreciated in 2005 to US$1=ZK3 508.9 (The Economist Intelligence Unit, 2007a:5, 2007b:44; Africa Confidential, 2006:4). Policies that the central bank and the Commerce, Trade and Industry Ministry introduced in 2003,[211] limiting services from being quoted in foreign currencies, also contributed to some stability in the kwacha in recent years (Bank of Zambia, cited in Africa Research Bulletin, 2003c:15633). The depreciation of the kwacha in 2006 to US$1=ZK4 406.6 was largely as a result of political uncertainty[212] and reductions in emerging-market premiums, owing to continued interest rate hikes in the major global economies that encouraged wide global emerging-market sell-offs (The Economist Intelligence Unit, 2007b:44).

[209] Consequent to the government's successfully implementing the majority of IMF-advocated reforms.
[210] Reflected in higher inflows of Zambia's two main sources of foreign exchange.
[211] To stop goods (including equipment).
[212] That plagued Zambia in 2006.

4.4.12 Foreign exchange reserves (excluding gold)

Figure 4.13 shows that the foreign exchange reserves increased slowly from 1986 until 1994. Thereafter, the reserves showed a general declining trend until 1999, when they reached their lowest level for the period covering 1980-2007. Subsequently, the foreign exchange reserves exhibited an upward trend and their growth accelerated during 2003-07. However, in the short term, under private ownership of all the copper mines, the foreign exchange reserves were volatile during 2000-03.

Donor assistance and foreign exchange generated from copper exports are the major variables affecting the level of foreign reserves in Zambia (The Economist Intelligence Unit, 2007b:44). Increases in donor support largely boosted the foreign exchange levels in 1985 during Kaunda's government, to US$200.1 million, from US$54.5 million in 1983 and augmented Zambia's foreign exchange in 1990 to US$193.1 million. Trade surpluses, alongside donors' contributions and debt relief, also contributed markedly to the considerable rise of Zambia's foreign exchange revenue in 1994.

Figure 4.13: Foreign exchange reserves

Sources: The Economist Intelligence Unit (2007c, 2008a:13).

The plummeting of the foreign exchange levels in the late 1990s to US$69.4 million in 1998 and to their lowest level in 1999 at US$45.4 million, was mainly owing to the prolonged aid freeze from donors in the latter part of the 1990s.[213] These measures followed Zambia's failure to meet certain IMF/World Bank benchmarks, including the privatisation of the ZCCM (The Economist Intelligence Unit, 2007b:44). The poor performance of the mining sector also contributed to the low exchange rates in the late 1990s.

The short-term volatility in the foreign exchange reserves between 2000 and 2003 under private ownership was possibly due to policies entitling private mining companies to repatriate 100% of their net profits from the sales of copper out of Zambia[214] and to the tendency of TNCs to withhold foreign currencies from the BoZ. These policies also limited higher foreign exchange reserves from mining under TNCs' ownership of the mines. Improvements in the trade deficit in 2002 underpinned the recovery of the foreign exchange in that year.

The reserves declined dramatically to only US$247.7 million in 2003 from the 2002 level of US$535.1 million (Africa Research Bulletin, 2001c:14687; Van Buren, 2003:1151). The worsening of the trade deficit in both 2001 and 2003 contributed to the decreases in the foreign exchange reserves in those years (The Economist Intelligence Unit, 2007c). The decline in external programme assistance in 2001 was also responsible for the reduction of Zambia's foreign exchange reserves in that year (PRSP, 2002:10; Van Buren, 2003:1156).

The increase in the foreign exchange reserves of Zambia to a more sustainable level in more recent years, from US$248 million in 2003 to US$1 090 million in 2007, were partly as a result of its improved balance of payments. The more favourable balance of payments were to some extent influenced by the surge in copper exports, following high copper prices, and various aid or balance of payments support extended to Zambia,[215] rather than because of the privatisation of the mines. More crucially though, the huge foreign debt forgiveness that Zambia enjoyed through its HIPC status and of even

[213] Forcing the government to draw down its reserves to meet debt-service payments and other obligations.
[214] Interview with John Lungu, 12 November 2003.
[215] The debt forgiveness reduced the interest payments of Zambia from US$144 million in 1999 to US$89 million in 2000 (The Economist Intelligence Unit, 2002:50).

greater significance, the MDRI, accounted for the significant increases in the foreign exchange levels from 2004 to 2007.

Accordingly, in addition to strong copper exports, inflows of aid assisted considerably in the build-up of the foreign reserves of Zambia at the BoZ,[216] especially in more recent years, as a large portion of the net surpluses from mining is repatriated out of the country (The Economist Intelligence Unit, 2008a:5). Despite the significant increase in the foreign exchange reserves to their highest level in the period covering 1980-2007, at US$1 090 million in 2007, the BoZ could nevertheless still cover only 2.7 months of imports (The Economist Intelligence Unit, 2007a:3, 2007b:43, 44).

4.4.13 Debt of Zambia

The surplus on the current account that Zambia enjoyed in 1974 was turned into an external debt of about US$1.7 billion in 1975 that increased enormously to US$6.6 billion in 1989, of which US$1 billion was comprised of overdue interest payments (Cherv, 1989:127; The Economist Intelligence Unit, 2007c). Zambia's foreign debt rose further to almost US$6.9 billion in 1990, demoting the country to one of the most indebted in sub-Saharan Africa. Only Sudan rivalled Zambia among Africa's problem debtors in 1989 (World Bank, 1996:3; Cherv, 1989:127; Leistner, 1996:11.18, 11.19; The Economist Intelligence Unit, 2007c).

Despite several debt relief initiatives from donors since 1991 immediately following MMD rule (such as debt cancellations, other debt relief and aid), which lowered the external debt of Zambia, the decreases in debt remained small and were unsustainable until 2005. For instance, the declines in Zambia's debt in 1994[217] (mainly owing to donors' contributing US$3.2 billion to the country and because Zambia's creditors at the time wrote off US$1.3 billion of the country's debt)[218] and in 2000 to US$5.7 billion were met in both instances by subsequent increases in Zambia's external debt (Leistner, 1996:11.18, 19; The Economist Intelligence Unit, 2007c). From Figure 4.14 it is noted

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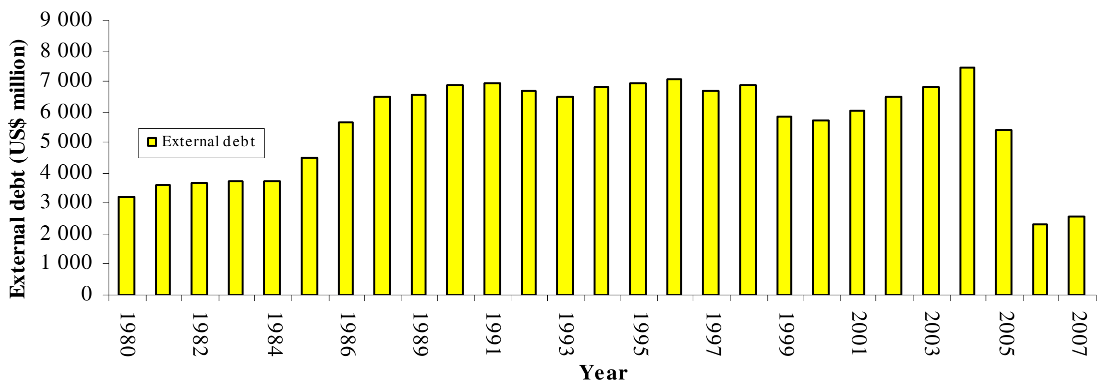
216 The BoZ would, though, intervene in the market to mop up excess liquidity (The Economist Intelligence Unit, 2008a:5).
217 That represents 184.5% of GDP and 549.9% of exports.
218 Totalling US$3.5 billion from 1992-94.

that Zambia's debt increased to US$7 billion during 1995-96,[219] ranking it then amongst the most indebted countries in the world (Leistner, 1996:11.19; Burnell, 1995:688; The Economist Intelligence Unit, 2007c).[220] Also, the country's debt peaked at US$7.3 billion in 2004, despite the approval of the three-year SDR220 million (US$320 million) poverty reduction and growth facility (PRGF[221]), in June 2004 (The Economist Intelligence Unit, 2007c).

Figure 4.14: External debt of Zambia



Sources: The Economist Intelligence Unit (2007c, 2008b:18).

The high aid statistics of Zambia[222] were not unique amongst low-income countries. What distinguished Zambia, however, was its huge debt service burden, with the interest payments on external debt then constituting the main income account debit.[223] The debt service of Zambia was US$70 million in 1998, US$144 million in 1999 and US$89 million 2000.[224] The debt service still constituted more than 37% of the country's foreign currency reserves in 2000 (Fraser & Lungu, 2007:60; The Economist Intelligence Unit, 2002:13, 50; Regional Investor Survey, 2001:37).

The debt stock of Zambia dropped significantly only from 2005, when the IMF and the

[219] Equivalent to 170% of gross domestic product.
[220] In 1993, external debt equalled 232% of GNP and no less than 638% of total exports, while debt service absorbed 32.8% of export earnings (down from 51.1 per cent in 1991).
[221] The main goal of Zambia's three-year PRGF with the IMF, due to run until September 2007, was to improve fiscal discipline and management, while other priorities under the PRGF were to improve governance, develop the business environment for the private sector and to complete the privatisation programme (The Economist Intelligence Unit, 2007a:2).
[222] Constituting 63% of the share of its GNI in 1995 but dropping to 21% in 2004.
[223] Principal repayments appear as a current transfer debit.
[224] There was a corresponding over 4% reduction in the 2001 income account deficit to US$168 million from its 2000 level (The Economist Intelligence Unit, 2002:50, 2007c).

World Bank formally endorsed a US$3.9 billion debt-relief package for Zambia,[225] under the HIPC initiative, in April 2005. The debt stock decreased sharply from US$7.1 billion (before Zambia received the HIPC partial debt relief package) to US$4.5 billion, immediately after the partial debt forgiveness it gained from the HIPC debt relief package[226] (Fraser & Lungu, 2007:60; The Economist Intelligence Unit, 2007b:43, 26, 2007c).

Better still, under the MDRI[227] that the World Bank and the IMF announced in 2006, those sub-Saharan African countries that had already reached the HIPC Completion Point won a massive additional write-off. The write-off entailed the IMF, the International Development Association of the World Bank and the African Development Fund (AfDF) cancelling 100% of their debt claims on Zambia. The debt cancellation under the MDRI,[228] reduced Zambia's external *public* debt stock to US$502 million in July 2006, according to government estimates less than a tenth of its previous level (Fraser & Lungu, 2007:6; The Economist Intelligence Unit, 2007b:43-44, 2008a:10, 2008b:24). The huge external debt forgiveness granted to Zambia, especially under the MDRI in 2006 enabled the government to build up its foreign-exchange reserves and to bridge the persistent substantial deficit on the current account that left a significant financing gap (The Economist Intelligence Unit, 2008a:10, 11, 2008b:24).

However, Zambia immediately started building up its loans again, resulting in a rise in its external debt from US$2 325 million at the end of 2006 to US$2 596 million in 2007,[229] mainly to finance the Fifth National Development Plan (FNDP),[230] running from 2006 to 2010 (Fraser & Lungu, 2007:61; The Economist Intelligence Unit,

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225 Subsequent to Zambia’s fulfilling almost all of the 15 key reforms and objectives set by the IMF to qualify for debt cancellation (The Economist Intelligence Unit, 2007b:43).

226 The debt, though, increased again and was already at the end of 2005 US$5.7 billion.

227 Born out of an acknowledgement that the HIPC scheme had failed to have the desired impact on the debt burden of many poor countries.

228 Involving the IMF’s writing off around US$577 million, the AfDF about US$245 million and the World Bank about US$1.88 billion.

229 That would cover just over half of the expected financing gap (equivalent of about US$1.5 billion) between projected costs, amounting to K65.2 trillion and projected domestic resources, estimated at K49.9 trillion, over a five-year period. Most of this funding should come from normal expenditure and funds previously budgeted for debt servicing but released by the MDRI deal (Fraser & Lungu, 2007:61).

230 The borrowing to finance the FNDP would culminate in a 66% hike in aid from both domestic and external sources, from an average of US$550 million per year, from 2004-2006, to an average of at least US$800 million for the five years of the FNDP (Fraser & Lungu, 2007:61).

2007a:2). Zambia's foreign *public* debt doubled to US$l billion by 10 June 2008 from the 2006 level. This is nevertheless still less than a seventh of its external debt in 2004. In 2007, the domestic debt of Zambia constituted 19.9% of GDP, compared to 129% of real GDP in 2000 (The Economist Intelligence Unit, 2008a:4, 10, 11, 2008b:24; Regional Investor Survey, 2001:37).

4.4.14 Inflation

The study uses the changes in consumer prices as an indicator of the inflation rate in Zambia, as data on changes in producer prices of Zambia are not readily available and consumer prices constitute the main variable affecting the inflation rate in Zambia. The terms 'inflation rate' and 'changes in consumer prices' are therefore used interchangeably in the study. A huge discrepancy exists between the official and unofficial inflation rates in Zambia, especially in the early 1990s. A high inflation rate harms local business profitability in particular and negatively affects the welfare of the nation, rendering it difficult for Zambians to afford basic goods.[231]

Figure 4.15 shows that the gradual increases in the inflation level, from 3.1% in 1964 to 20% in 1984, were followed by a considerable rise and a higher volatility in inflation from the late 1980s and especially in the early 1990s until 1993. Inflation that averaged 44% from 1985 to 1987 increased to 55% in 1988, subsequent to the abandoning of the economic reform programme in 1987 (World Bank, 1996:13; The Economist Intelligence Unit, 2007b:31). The high increase in inflation in 1991, at 98.5%[232] was largely as a result of the Kaunda government printing more money to meet the 100% increase in the salaries of civil service employees and to pay for the election campaign,[233] following the IMF's suspension of all financial disbursements to Zambia (Simutanyi, 1996:828).

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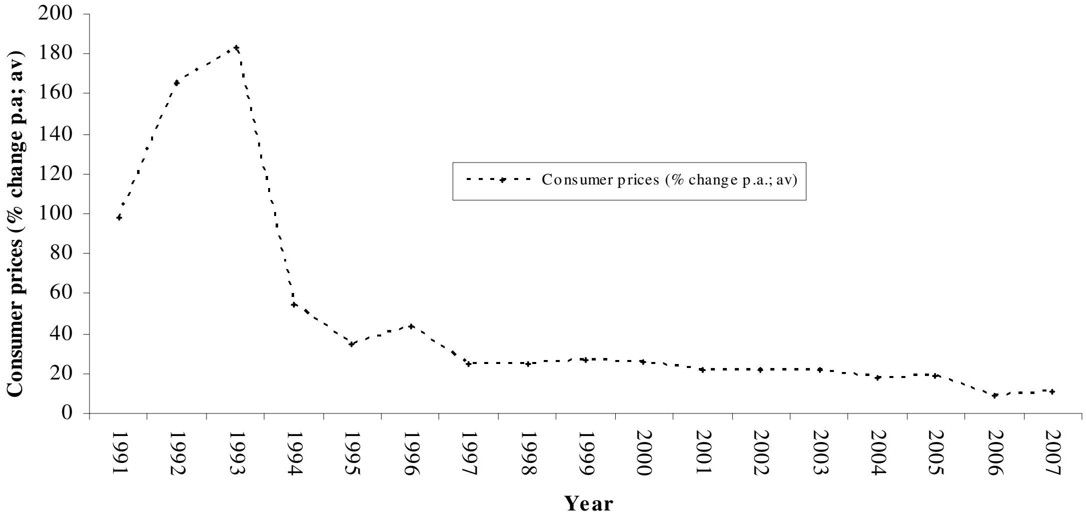
[231] On the other hand, most international companies in the export sectors of Zambia that benefit from higher dollar and rand rates over the kwacha, are less affected by the increases in the consumer price index. These companies tend to act against the effects of inflation by hedging against the depreciation of the kwacha, partly, by keeping most of their income in dollars and rands.

[232] The unofficial inflation rate was purported to be 400% (Van Buren, 2003: 1155).

[233] While government spending in productive activities (like construction, building the capacities of local companies and agriculture) or development projects would promote economic growth (even though it would contribute to some increases in inflation), the injection of government borrowings mainly in unproductive, consumption orientated sectors, such as for salaries, wages and for recurring departmental charges, would crowd out the private sector (interview with Fred Yamba, 25 November 2003).

Figure 4.15: Percentage change in consumer prices



Sources: The Economist Intelligence Unit (2007c, 2008b:18); Bank of Zambia (2000).

At the beginning of MMD rule, the inflation level increased even further to 165.7% in 1992 and peaked at 183.3% in 1993. Subsequently, it dropped sharply to 54.6% in 1994. The inflation level has stabilised since 1998, when it reached 24.5% and ranged between 26% (in 2000) and 18% (in 2004) in the 1999-2004 period. In 2006 inflation declined considerably to 9%.

The main factors that accounted for the high inflation in Zambia, especially at the start of MMD rule, were the loose monetary policy, which historically allowed the value of the kwacha to fall and that in turn encouraged inflation and rising import costs, especially of fuel; a weak exchange rate;[234] lax fiscal policy; and inconsistent food supplies (The Economist Intelligence Unit, 2002:35; ZPA, 2000a:16). One of these conditions is sufficient to stoke inflationary pressures (The Economist Intelligence Unit, 2002:35, 2007b:31, 2008b:22).[235] The demand management programme that SAPs promote largely accounted for the decline in inflation after 1993 under MMD rule. The stronger currency influenced the drop in inflation to 9% in 2006, in addition to a combination of prudent fiscal policy and a bumper maize crop (The Economist

[234] Firmer monetary control demanded from SAPs since 1994 and policies aimed at encouraging greater exchange rate stability possibly also promoted the decline in inflation from 1994 (Africa Research Bulletin, 2001e:15009; IMF, cited in Van Buren, 2003:1155-1156).

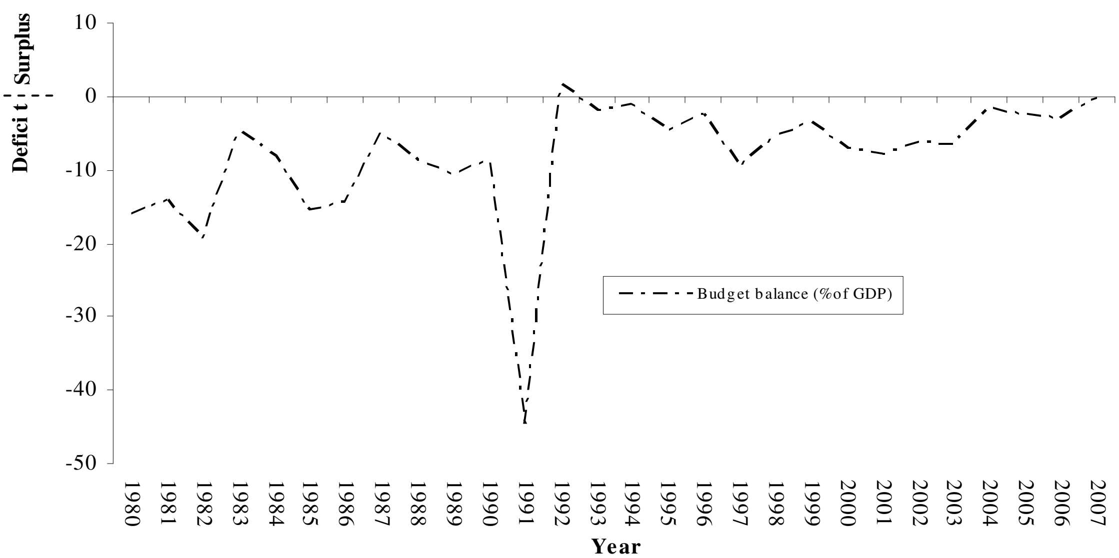
[235] The consistency of food supplies is largely determined by the success of the maize harvest.

Intelligence Unit, 2007b:31, 2008b:22).

4.4.15 Budget deficit

Figure 4.16 shows that Zambia experienced a higher budget deficit during Kaunda's government than under the MMD government, mainly because of the greater government expenditure linked to Kaunda's humanist policies. The stricter adoption of SAPs of the Chiluba government, in comparison with the Kaunda government, which limited government expenditure, curbed somewhat the budget deficit of the MMD government. In the period covering 1980-2007, the highest increase in the budget deficit in 1991 at 45.1% of GDP from 8.7% in 1990 was principally due to the excessive spending of the Kaunda government on its election campaign and because of the 100% increases in the salaries of civil service employees, to promote electoral-maximising motives.

Figure 4.16: Budget balance (as % of GDP)



Sources: The Economist Intelligence Unit (2007c, 2008a:7).

While the budget deficit was generally lower during the MMD government, who also enjoyed a brief budget surplus of 1.5% in 1992, the deficit nevertheless displayed an increasing trend from 1993 to 2003. The budget deficit from 1994 to 2004 averaged around 5.5% of GDP. Government spending on recurrent charges, such as wages and salaries and loss-making parastatals, rather than on capital projects (that would have had more positive outcomes on Zambia's development), affected the budget of the country in a negative fashion. The increases in the budget deficit from 1994 to 2003 were also mainly as a result of donors failing to disburse the amount of aid they had pledged, according to the MMD government (The Economist Intelligence Unit, 2007b:28).

However, since 2004, the budgetary performance has been more favourable, with the fiscal deficit dropping to only 1.7% of GDP in 2004, down from 6.6% in 2003, owing to the improved fiscal management, focused on enabling Zambia to qualify for the new PRGF (The Economist Intelligence Unit, 2007b:28, 2008b:17). The budget deficit also improved considerably in 2007 to only 0.3% of GDP, from 2.9% in 2006. The significant increases in the budget of the Finance Ministry to US$3.2 billion by the end of 2005 were spurred mainly by the copper boom and the enormous decline in the debt of Zambia. In turn, this enabled the government to potentially finance 71% of the 2006 budget of Zambia from local resources (Africa Confidential, 2006:4).

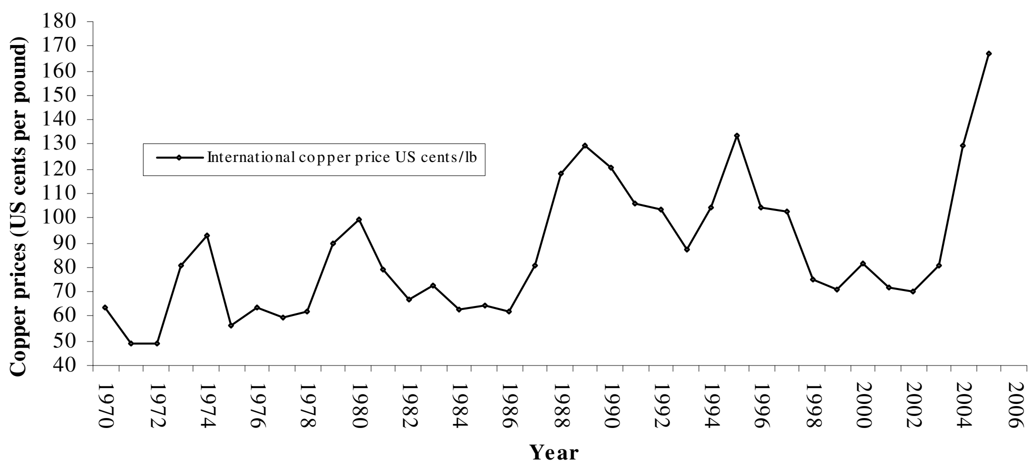
4.4.16 Copper prices

The price of copper shows high volatility (refer to Figure 4.17) and declined in the last three decades by an average annual rate of about 3.4%. The Zambian economy's enormous dependence on copper renders its performance highly vulnerable to the price of copper and, by extension, to the demand for the commodity by major industrialised consumers, since international demand and supply factors largely determine the price of copper. The performance of the Zambian economy is therefore highly sensitive to the strength and duration of world recovery, especially of the USA (that consumes more than one quarter of the world's minerals) and more recently of China, that has replaced the USA as the world's largest consumer of copper (The Economist Intelligence Unit, 2007b:42; Africa Research Bulletin, 2003d:15677; Ministry of Finance and National Planning, 2002b:74, 75; The Post, 2003a:4).

Accordingly, the two major world recessions, viz. 1973-75 and 1979-82, depressed the demand for and the price of copper in 1975 and 1982. The general low copper prices in the 1980s were also attributable to the flooding of the world market for copper, as a result of the policies of the IMF that encouraged the copper-producing developing countries to increase their copper exports – a policy that proved harmful to Zambia's economy (Cherv, 1989:136; Seidman, 1977:236).

The plummeting of the price of copper by 44% from mid-1997 until 2002 was mainly attributable to the 1997-98 Asian crisis,[236] the subsequent contagious ripple effects that precipitated the Russian and Brazilian financial crises, and the 11 September attacks in the USA in 2001 (Africa Research Bulletin, 2001d:14976; Ministry of Finance and Economic Development, 1999:47, 2001:74; Ministry of Finance and National Planning, 2002b:74, 75, 2003:28; ZCCM, 1999:7). The doubling of Western commercial stocks over the 1997-98 period to 1.2 million tons further depressed the price of copper in the late 1990s (Ministry of Finance and National Planning, 2002b:75). The copper price declined from US102.5 cents/lb in 1997 to US71.1 cents/lb in 1999.

Figure 4.17: Copper prices*



*Exclude outlier in 2006, when copper prices peaked at 305.6 US cents/lb.

Sources: *Adapted from IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:13); The Economist Intelligence Unit (1989-90:37, 1995-96:34, 1999-2000:24, 2001:33, 2006:41, 2007b:35).*

However, after decades of a general decline (except for the brief respite in 1994/1995 when the price of copper was significantly higher than the long-term trend) the global

[236] That accounted for the poor economic performance of Japan and South East Asia.

price of copper rose to unprecedented levels between 2004 and 2006. The copper price increased from US80.3 cents/lb in 2003 to US305.6 cents/lb in 2006 (World Bank, 2004a:48). The major catalysts for the increases in the price of copper from 2003 to 2005 were the tight supply of copper-producing countries and high global demand (especially by China), riding on strong world economic growth, as the world economy was coming out of a recession, which benefited the commodities market.[237] Threats of industrial action and speculative pressure further contributed to the higher copper prices in 2006 (Fraser & Lungu, 2007:1, 2; The Economist Intelligence Unit, 2007a:4, 30, 2008a:6).

Nonetheless, the long-term trend in copper prices, expected to move cyclically in tandem with world economic demand, is likely to remain negative. This is partly because structurally, the copper mining industry is subject to a significant degree of product substitution,[238] which will depress demand and consequently the price of copper (World Bank, 2004a:48). In the absence of a greater diversification of the Zambian economy, such a trend would impact negatively on the country's livelihood. Government policies aimed at diversification therefore appear necessary to relieve the economy of its huge dependence on the highly volatile copper prices that create a lot of uncertainty, and to eliminate the 'Dutch disease' that afflicts Zambia.

4.4.17 Copper production

The copper production levels are considered in some detail below, to illuminate the factors that account for the trends in copper production, discussed in Section of 5.4.1.1 of Chapter 5. In the late 1960s and in the 1970s, Zambia was among the top global copper producers. It is noted from Figure 4.18 that broadly, the copper output declined more significantly in the 1980s than in the 1970s. The decline accelerated in the 1990s. Production levels increased again, albeit slowly, in the short term under private ownership of the mines.

More specifically, in the 1960s copper production increased dramatically to

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237 Interview with Valentine Chitalu, 22 October 2003.
238 Especially by fibre optics.

680 000 tons in 1965 from 350 000 tons in 1955. Zambia's copper production levels peaked in 1969 at 747 500 tons, accounting then for 12% of international production (Van Buren, 2003:1152; The Economist Intelligence Unit, 2007b:34). The opening of new ore sources[239] largely accounted for the phenomenal growth of copper production in Zambia from the late 1950s until 1969 and for its continued high levels in the mid-1970s (Maambo, 1998:5; The Economist, 2002b:1). The significant decline in the production of copper from its peak in 1969 to 534 600 tons in 1971 was mainly attributable to over a million tons of mud and water from the surface engulfing a large part of the underground workings of the Mufulira Mines[240] (Maambo, 1998:5).

Despite subsequent declines in the production of copper from levels attained in 1969, the production levels remained high until 1976, when it still reached about 700 000 tons. A combination of factors, viz. a depressed copper price from late 1974 to mid-1978, the hike in the oil price, the effects of political turmoil in Southern Africa that spilled over into Zambia and the higher turnover of the expatriate personnel contributed to the poorer performance of the mining sector from 1977-79. Limited foreign exchange and the scarcity of spare parts further precluded better performance in the latter part of the 1970s (Roan Consolidated Mines Limited, 1980:4).

In the 1980s, production levels declined considerably from 607 200 tons in 1980 to 448 400 tons in 1989. The lower production levels in the 1980s were caused by: delays in promised foreign exchange from donors from 1983 to 1986; the closure of high-cost and less profitable mines in 1987[241] and of the Luanshya smelter and the Ndola copper refinery; shortfalls in foreign exchange; and higher costs[242] of mining (World Bank, 1989:49; Maambo, 1998:Fig. 8). During the late 1980s, the costs profile of the ZCCM escalated from the lower to the upper decile of the world's producers (Maambo, 1998:Fig. 8). The high costs at the time were mainly owing to the significant depreciations of the kwacha in 1987, subsequent to the auctioning of the foreign

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[239] Namely, the Nchanga Open Pit and Konkola in 1957, the Chibuluma mine in 1963, the Chambishi Open Pit in 1965 and the Kalengwa mine in 1969.

[240] Which cost the lives of 69 miners in September 1970.

[241] Namely Chambishi, Konkola No.3 Shaft and Kansanshi.

[242] Beyond those of most global competitors.

exchange rate in 1986 that, in the absence of local substitutes, increased the price of mining inputs. The more expensive methods of mining required for deeper level mining and the poorer average grade linked to deeper copper ores further contributed to the high increases in the costs of mining input from 1985 to 1987 (Cherv, 1989:127; Maambo, 1998:Fig. 7).[243]

The acceleration of the decline in the average copper production in the 1990s during Chiluba's rule was at a rate of about 5.1% p.a., compared to the 3.5% long-term decline (World Bank, 2002b:9, 2003b:134, 2004a:48). The levels of copper production dropped in the 1990s (except for the brief increases in 1992 and in 1993) from 448 400 tons in 1989 to 382 000 tons in 1991, to only 260 000 tons in 1999. The general decline in the production of copper in the 1990s, despite the higher copper prices in 1994 was predominantly due to high production costs.

The increases in production costs in the Copperbelt region[244] in the 1990s were again mainly as a result of the depreciation of the kwacha and the high costs associated with deeper level mining and the lower grade of copper, together with geological factors[245] and increased seismic activities (ZCCM, 1996, cited in Lungu & Silengo, 1997:26; Ministry of Finance and National Planning, 2002b:75; Maambo, 1998:Fig. 1). Underinvestment in the mines, significantly the outcome of pressure from the IMF and the World Bank that the government limited its investments in the mines that were earmarked for privatisation[246] further increased production costs (Andersson, 2000:75). Shortages of low matte grade concentrates at the Mufulira smelter and of acid and low acid soluble copper in tailings, which resulted in many unscheduled shutdowns, added to the drop in production levels in the late 1990s (ZCCM, 1999:11).

In 2000 when all the mines were transferred to private ownership, copper production

[243] Shortages of largely imported spare parts in the mining and in the metallurgical processing plants, linked to the lower accessibility of foreign exchange to Zambians, following the depreciation of the kwacha, contributed to the importing of machinery into Zambia dropping to only 4.6% in 1986 (from 13.4% in 1984) of a declining total foreign exchange base. This resulted in a deferring of mining projects that would have replaced declining reserves (Africa Now, 1987:31; Maambo, 1998:Figs. 7, 8).

[244] By about 50%, with the increasing replacement of high grade minerals bornite and charcocite by low grade mineral chalcopyrite, as the mines deepened.

[245] Such as the reduced strike lengths, thickness and shallow dip of ore bodies that rendered the caving method inappropriate.

[246] Interview with Zion Simwanza, December 2003.

dropped to only 257 000 tons,[247] its lowest level since the late 1950s (The Economist Intelligence Unit, 2002:40, 2007b:34; Ministry of Finance and Economic Development, 2000:60; Fraser & Lungu, 2007:19). The decline was largely attributed to delays in the arrival of spare parts and equipment; the state of dilapidation of the mines; industrial and labour unrest (also in 1999); and the drop in copper production[248] at Roan Antelope Mining Corporation of Zambia (RAMCOZ) (Ministry of Finance and Economic Development, 2000:60; Lungu, 2001:15; Mining Journal 17/11, cited in Africa Research Bulletin, 2000b:14593). Disruption in acid supply at KCM in the first quarter of 2001, as well as increased water levels in the mines and the placement of RAMCOZ under receivership contributed to the rather low copper production levels in 2001 (Ministry of Finance and National Planning, 2003:22; The Economist Intelligence Unit, 2002:41).

Production levels indicate an increasing trend under private ownership of the mines from 2001. The increase has become more significant, from 2004-2007. The higher copper production in 2002 to 337 700 tons, despite the withdrawal of Anglo American from KCM in 2002, was mainly due to the recapitalisation of the mining sector and the boost in the production of copper at Bwana Mkubwa (Ministry of Finance and National Planning, 2002c:62; Pretoria News, 2004:21; Regional Investor Survey, 2001:38; Africa Analysis, 2001:12; Africa Mining Intelligence, 2002b:1).[249]

Copper production in Zambia almost doubled to 497 100 tons in 2006, from 257 000 tons in 2000. The value of metal exports rose from US$506 million in 2001, to over US$1 billion in 2005 and to US$2.7 billion in 2006 (The Economist Intelligence Unit, 2007b:19, 25, 30, 34; Fraser & Lungu, 2007:1, 19; Africa Confidential, 2006:5, 2007:10). Nevertheless, these levels remained lower than those attained in the 1960s and early 1980s under Kaunda's government.

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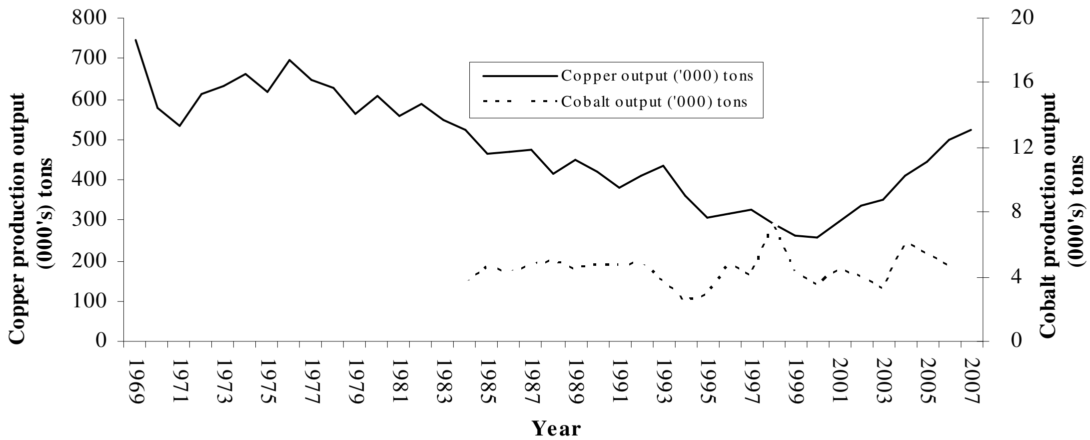
247 With KCM then producing only 136 000 tons of copper in the nine months of its operations.

248 From 3 000 tons to 1 000 tons a month.

249 Production at Bwana Mkubwa increased from 2 500 tons per annum to about 30 000 tons in 2002, assisted by the increasing ores that First Quantum acquired from the Lonshi copper mine in Congo-Kinshasa, that are processed at Bwana Mkubwa, whose ore reserves in Zambia were almost exhausted in 2001 (interview with Andrew Hickman, 7 November 2003).

Figure 4.18: Copper and cobalt production



Sources: Adapted from IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:13); The Economist Intelligence Unit (1989-90:37; 1990-91:27; 1995-96:21, 34; 1999-2000:24; 2000:46; 2003:47, 63; 2006:65; 2007b:35; 2008b:19); Van Buren (2003:1152).

Record high international copper prices between late 2004 and 2006, the massive rehabilitation works undertaken in 2004, in particular at KCM and at MCM, and higher investments in expanding production and mining sector growth[250] spurred the significant rebound in copper production levels in more recent years. However, extensive floods, industrial action, insufficient capacity for processing concentrates in Zambia, shortages of fuel and the 10-day closure of the KCM leaching facility[251] contributed somewhat towards the unexpectedly lower levels of copper production in 2007, at 521 984 tons (Bantubonse, cited in Africa Mining Intelligence, 2006b:2; The Economist Intelligence Unit, 2007b:30).

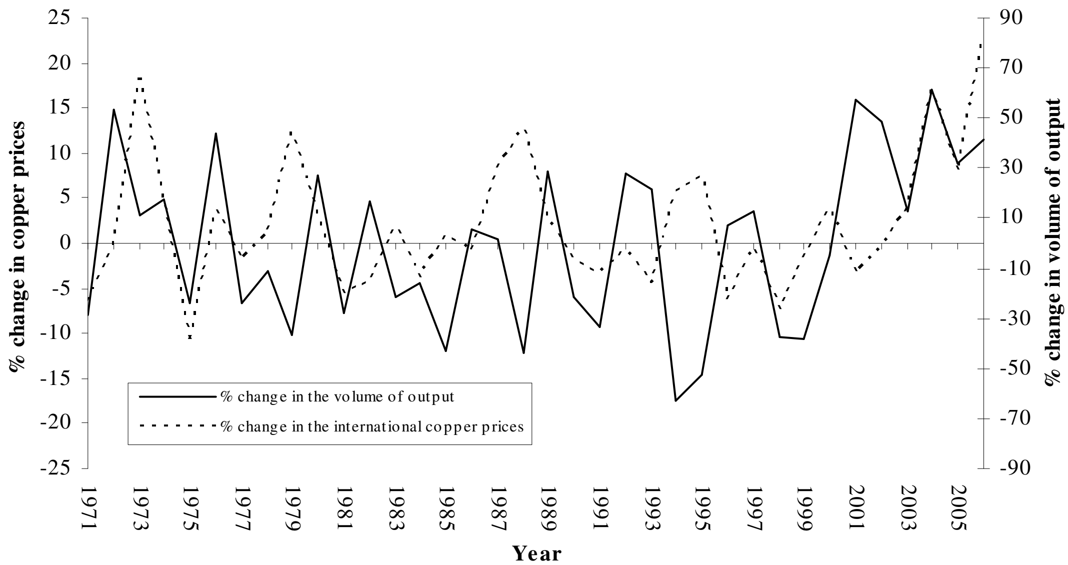
4.4.18 Volume and price of copper

Figures 4.19 and 4.20 show that in the 1970s and the 1980s, under Kaunda's government, a correlation existed for the most part in the responsiveness of the supply of copper to price (or the supply elasticity of copper). Accordingly, price significantly determined copper output. The high responsiveness is reflected in the sharp increases and decreases in the volume of copper within short periods following fluctuations in the price of copper under Kaunda's government, compared to the 1990s under Chiluba's

[250] The latter of which increased by almost 50%, in real terms, from 2001 to 2005.
[251] To address the pollution problems that the mine experienced.

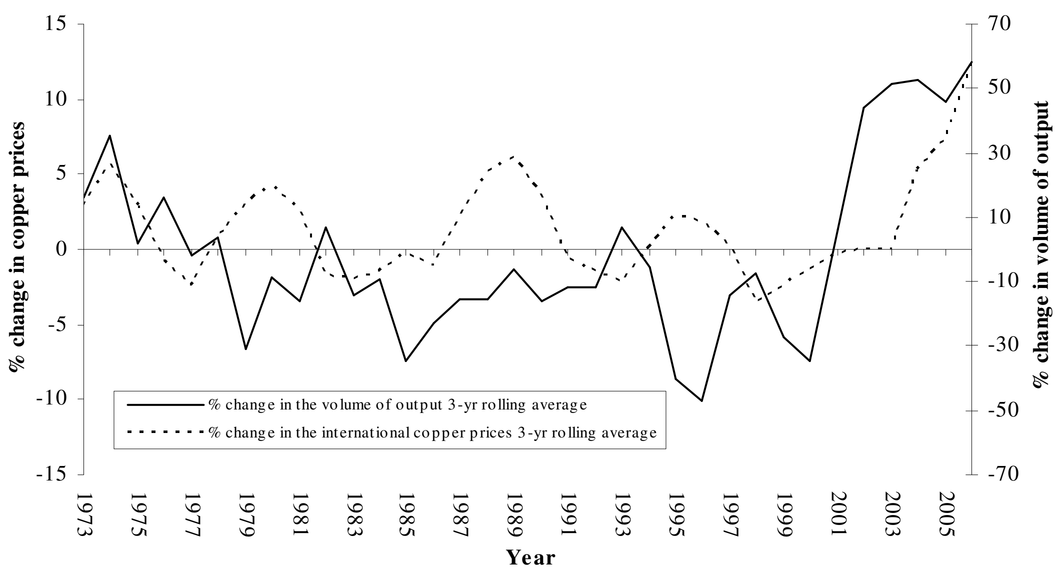
government.

Figure 4.19: Changes in volume and price of copper



Sources: Adapted from IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:13); The Economist Intelligence Unit (1989-90:37; 1990-91:27; 1992-1993:26; 1995-96:21, 34; 1999-2000:24; 2003:47; 2006:65; 2007b:35); Van Buren (2003:1152).

Figure 4.20: Changes in volume and price of copper (rolling averages)



Sources: Adapted from IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:13); The Economist Intelligence Unit (1989-90:37; 1990-91:27; 1992-1993:26; 1995-96:21, 34; 1999-2000:24; 2003:47; 2006:65; 2007b:35); Van Buren (2003:1152).

Instances during Kaunda's government when the volume of copper did not respond to falling copper prices (in 1982 and 1989) possibly reflected, among other, policies of the Kaunda government to at times cushion production levels under state ownership to prevent massive changes in employment. On the other hand, it is noted from Section 4.4.17 that the oil crisis, the spill-over effects of the political turmoil in southern Africa and constraints in foreign exchange largely accounted for the poorer response of the mining sector to increases in the copper price in the latter part of the 1970s (Roan Consolidated Mines Limited, 1980:4). Moreover, the higher production costs and lower grade of ore and the closure of several mines in 1987 contributed to the lower copper production levels in 1988, despite increases in the price of copper. Clear conclusions of asymmetric responses in production to increases and to decreases in copper prices could not be drawn within the confines of the study.

In the 1990s, under Chiluba's government, two notable trends marked the relation between changes in the volume of copper output and those of relative copper prices. The trends were likely significantly influenced by strict SAPs and liberalisation policies that were introduced and by the uncertainty as to the fate of mining (after the mid-1990s) before the change to private ownership of the mines. Firstly, the supply elasticity of copper was much less elastic than under Kaunda's government, indicating that the volume of copper was not strongly driven by price during this period. On the contrary, from 1994-97 the changes in the volume of copper output and in the price of copper moved in opposite directions with output falling in 1994 despite the increases in the price of copper in 1994-95. Secondly, the plunges in copper production lasted longer in the 1990s.

The resistance in the output response to the changes in the price of copper from the mid-1990s was considerably influenced by the lack of resources and policies of the IMF and the World Bank discouraging investment in the mines earmarked for privatisation. In addition, the increasing costs of production in the 1990s obstructed higher production levels, restricting greater gains for Zambia from higher copper prices. The long time it took to finalise the privatisation of all the major copper mines, in the absence of adequate reinvestment of the mines, also proved disruptive to growth in copper production. However, in 1998 and 1999, when some of the mines were already privatised, the supply elasticity increased.

Under private ownership of all the mines from 2000 a stronger positive correlation existed in the changes in the volume of copper output and the price of copper from 2003-06 compared to under Kaunda's government and much more so than in the 1990s. This demonstrates a greater short-term responsiveness of the private owners to price changes. The negative relation from 2000-02, namely a rise in growth in the volume of output when copper prices declined was likely as a consequence of the initial positive impact of higher investments into the mines under private ownership. However, the greater responsiveness in the volume of output to price under private ownership from 2003-06 corresponded to the period of unprecedented high copper prices confounding definitive conclusions as to the role of ownership on the elasticity of supply. Moreover, the longer-term responses of copper output to copper prices under private ownership did not as yet play out since the mines were fully privatised only in 2000.

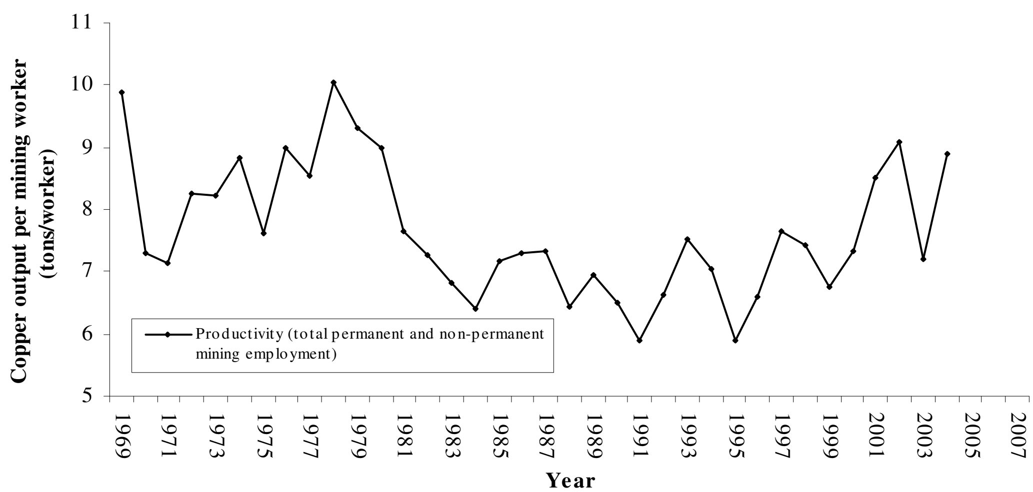
On the flipside, production decisions of mining companies in Zambia had an insignificant impact on the international copper price in the 1990s and in the 2000s, as Zambia's copper output contribution to the international stockpile was small during these times. The output level of Zambia's copper to the total world production was only 4.6% in 1990 and it declined even further to a mere 1.94% in 2000. At the height of the copper price boom in 2007, Zambia contributed only 3.37% to the international stockpile, compared to 12.58% in 1969 (The World Copper Factbook, 2009).

4.4.19 Productivity of workers in the mining sector

Figure 4.21 shows that the productivity of the mineworkers was on average higher in the 1970s than the 1980s. The average labour productivity in the 1990s also exceeded that of the 1980s but displayed considerable volatility. A more significant increase in the productivity of the mineworkers took place under private ownership of the mines.

More specifically, the peak in labour productivity in the mining sector in 1978, at 10 tons/worker, was primarily as a result of the considerable decline in the excess numbers of mineworkers (employment of mineworkers was reduced from 75 974 in 1977 to 62 650 in 1978), alongside relatively high production levels. However, the sizable drop in copper production and an increase in mining employment account for the lower productivity of workers in 1970 to 7.3 tons/worker, from 9.9 tons/worker in 1969. In the early 1980s, the significant fall in the productivity of the workforce in mining to only 6.4 tons/worker in 1984 was principally due to the considerable rise in employment levels in the mines (from 60 730 in 1979 to 81 982 in 1984) amidst declining copper production levels. The notable reductions in the excess workforce contributed largely to the subsequent higher labour productivity of 7.2 tons/worker in 1985.

Figure 4.21: Productivity of workers in the mining sector



Sources: Adapted from IMF Financial Statistics, World Bank World Tables, Central Statistical Office and Bank of Zambia (cited in Andersson, 2000:13); The Economist Intelligence Unit (1989-90:37; 1990-91:27; 1995-96:21, 34; 1999-2000:24; 2000:46; 2003:47, 63; 2006:61, 65; 2007b:35; 2008b:19); Van Buren (2003:1152); Central Statistical Office, Quarterly Employment and Earnings Inquiry and the Monthly Digest of Statistics (2006).

The rise in the average labour productivity in the 1990s, over that of the 1980s, was chiefly as a result of the huge reductions in the excess mining sector labour force that led to a more efficient use of the existing labour force. However, the lowest worker productivity levels between 1969 and 2007, of only 5.9 tons/worker, occurred in 1991 and in 1995. Higher increases in labour productivity in the 1990s were curtailed mostly by the large drop in copper production levels. In addition to lower production levels the reductions in the labour productivity of the mining sector in 1995 were also as a result of the uncertainty created by the impending privatisation of the ZCCM and the breaking down of corporate governance,[252] demonstrated in the Cobalt Report (Kapika *et al*., 1996:4).

The higher productivity levels of permanent workers in 2000 under private ownership of all the major copper mines, from 6.8 tons/worker in 1999 to 7.3 tons/worker in 2000, were mostly because of the more efficient use of an even lower number of the permanent workforce than in the 1990s, since production levels in fact dropped to their lowest levels in 2000. From 2002, higher copper production levels also accounted for the increase in the productivity levels of mineworkers. In 2002 productivity levels of the mines reached 9.1 tons/worker.

4.4.20 Government revenue from mining

Under private ownership and control of the mines during most of the 1960s, the high contribution of mining to government revenue in 1965 at 71% and in 1966 at 64% was mainly due to the boom in international copper prices and to the enormous taxes imposed on mining companies. The taxes amounted to about 73% of their profit.[253] Subsequently, government revenue from mining declined dramatically to only 13% in 1975 and to zero from 1977-79 (Fraser & Lungu, 2007:7).

However, despite the decline in the share of mining to government revenue to 58% in 1970 government revenue increased from US$365 million in 1966 to US$673 million in 1970 under government ownership but private sector management of the mines. The high copper production levels and the boom in world copper prices then accounted for the high government revenue (Seidman, 1977:224). The subsequent sharp decline in the contribution of mining to government revenue in the 1971-72 period, to only about US$65 million in 1972, when the mines were under government majority ownership but

[252] Interview with Sipho Phiri, 30 October 2003.
[253] Principally because taxation was based on production, rather than on profit.

still under private management, was chiefly owing to the drop in international copper prices. The rise in the costs of production,[254] the amendment in the legislation in 1969 that reduced the effective tax rate of the mining sector from 73% to 28% of profit,[255] as well as the fall in production,[256] further reduced government revenue in 1971/72 (McGrath & Whiteside, 1989:169; Seidman, 1977:224, 232, 233).

In the early 1980s, the negligible contribution of mining to government revenue, under the ZCCM, was mainly owing to losses that the mining sector experienced from 1982 to 1983 (Saasa, 1987:7; EDI, cited in the World Bank, 1989:19). The two subsequent tax regime changes within the 1980s significantly influenced government revenue from mining. The first change from a tax on profit to a mineral export tax, determined through the value of metal produced, applicable from 1983 to 1987, led to an increase in government revenue during these years. The percentage of the mineral export tax increased progressively[257] from 4% in April 1983 to 8% in August the same year and further to 10% from 1985-86 and to 13% in 1987 (ZCCM, 1983:10).

The higher mineral export tax contributed to the increase in government tax revenue from only US$5 million in 1982 to US$140 million in 1986, despite the decline in total revenue of the ZCCM from US$930 million in 1982 to US$680 million in 1986 (Maambo, 1998:8). The more favourable tax regime granted to the ZCCM after 1987, following the elimination of the mineral export tax on 1 January 1988,[258] together with the recovery in the copper price in late 1986, reduced government revenue but enabled the ZCCM to enjoy profits in subsequent years (Maambo, 1998:Fig. 8; ZCCM, 1988:4; Africa Now, 1987:31).

[254] Reportedly by about 20%. The higher costs were mainly attributable to (i) higher management fees, averaging about US$6-7 million per year, paid directly to the companies but which were added as an operating cost; (ii) companies over-invoicing imports from their own suppliers, which lowered the annual government revenue by about US$72 million; (iii) the huge compensation payments that the government made to the mining companies; (iv) the concession allowing companies, after deducting less than 30% for taxes, to repatriate a major share of their profits; (v) the practice of private mining companies to largely borrow abroad, for investment purposes, at 7% to 9% interest, instead of reinvesting their share of profits and (vi) the declining ore grades, requiring more expensive capital equipment to extract copper (Seidman, 1977:233, 234).

[255] Mainly through the replacement of the existing royalty and export taxes, which were based on the production of copper and sales, by a single mineral tax that was linked to a percentage of gross taxable profit, the policy exempting mining companies from paying taxes if losses occurred, and permitting companies to write off 100% of all investments in the year they were made, for tax purposes (which cost the government an estimated US$70 million in tax revenues in 1971 and 1972).

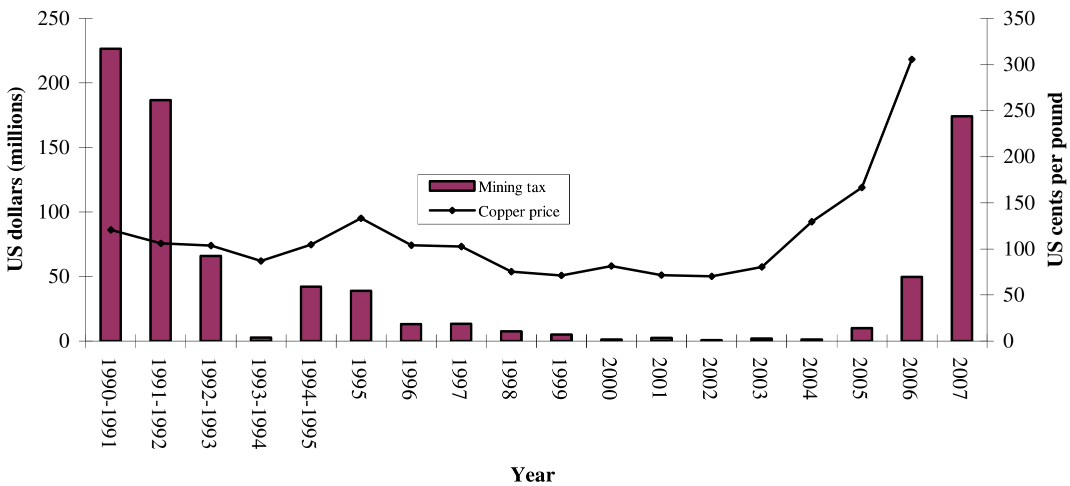
[256] Caused, primarily, by the cave-in at the AMAX-managed Mufulira mines.

[257] With the consent of the IMF and the World Bank.

[258] Saving the ZCCM approximately US$75 million in costs, per annum.

Figure 4.22 shows that taxes from mining were also considerable in the early 1990s, reaching about US$236.7 million in the 1990-91 financial year and US$194.6 million in the 1991-92 financial year. The higher mining revenue coincided with the introduction of the mineral export levy in 1990, which progressively increased the levy at copper prices over US$1.00/lb. Any revenues earned from prices over US$1.20/lb went to the government (Maambo, 1998:Fig. 8).

Figure 4.22: Government revenue from mining



**A financial year covered 12 months ending the 31 March.

Sources: Chamber of Mines, Unpublished presentation provided by Chairman of the Chamber to the IMF Visiting Mission to Zambia (cited in Fraser & Lungu, 2007:77); ZRA (2010);[259] ZCCM (1992:2, 1993:22, 1994:9, 1996:19).

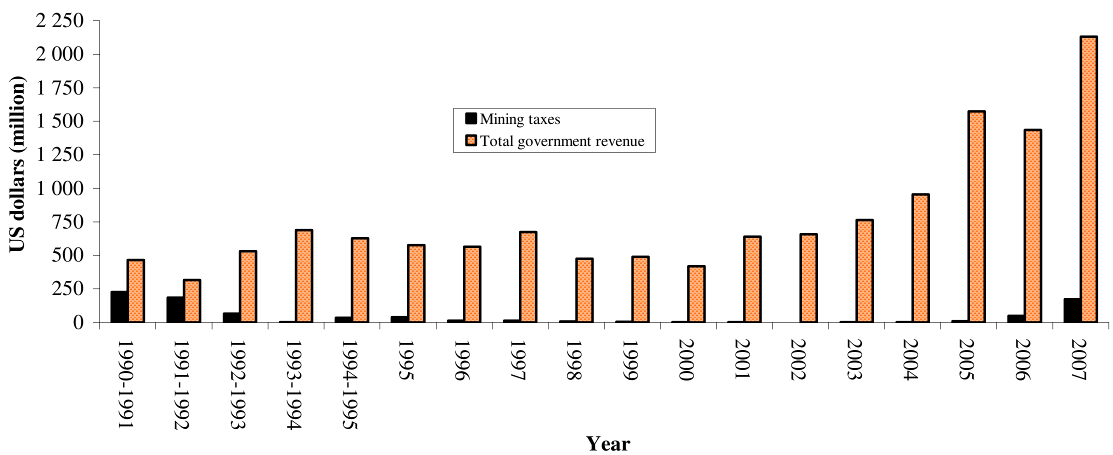
Subsequently, a significant drop in mining taxes took place. Losses that the ZCCM experienced in the 1993-94 financial year accounted for the fall in mining tax in that financial year to US$2.6 million. The abolishing in April 1994 of the mineral export levy that was replaced with a royalty on base metals tax (at a rate of 3%), the removal of exchange controls and reductions in taxation on both profits and imports influenced the downward trend in taxes from mining from 1994 to 1999 (ZCCM, 1994:7; Maambo, 1998:Fig. 9). Total mining tax was US$38.84 million in 1995. Net losses[260] that the ZCCM experienced from 1996 to 2000 also considerably influenced the additional

[259] Information sent on request.
[260] Amounting to about US$144 million in the 1996-1997 financial year (ZCCM, 1997:22).

decline in taxes from mining in the latter part of the 1990s.

Figures 4.22 and 4.23 show that in the short term under full private ownership of the mines, government revenue from mining taxes (excluding PAYE from mineworkers but including withholding tax, royalty tax and company tax) declined even further to negligible levels until 2004, from the low level of 1999 of US$5.2 million. The concessions granted to mining TNCs largely accounted for the poor mining taxes in the short term under private ownership of the mines. The contribution of mining taxes to total government revenue was still relatively low in 2005, at US$10.07 million, despite high increases in the price of copper. Subsequently, mining taxes rose to US$49.68 million in 2006 and to US$174.29 million in 2007.

Figure 4.23: Mining taxes and total government revenue



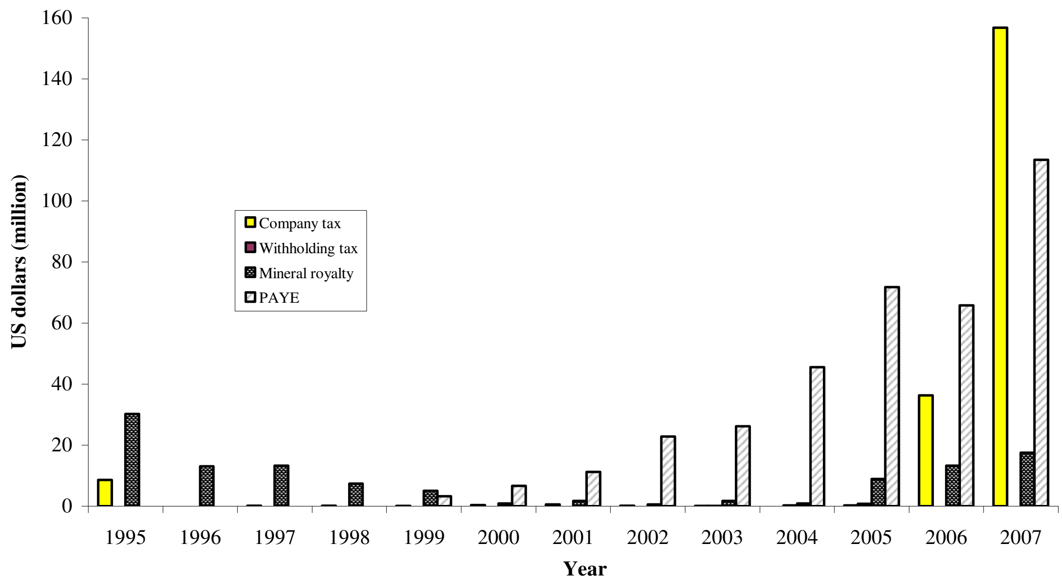
Sources: Chamber of Mines, Unpublished presentation provided by Chairman of the Chamber to the IMF Visiting Mission to Zambia (cited in Fraser & Lungu, 2007:77); ZRA (2010);[261] World Bank (2007); ZCCM (1992:2, 1993:22, 1994:9, 1996:19).

Figure 4.24 illustrates that within the mining sector, the taxes from mining employees, through PAYE, were the main contributor to government revenue under private ownership of the mines. The contribution by way of company tax, withholding tax and mineral royalties remained meagre until 2004. From 2000 to 2004, the government gained less than US$1.75 million in mineral royalties from mining TNCs, compared to US$7.44 million in 1998. At the height of the copper price boom, mineral royalties

[261] Information sent on request.

increased to US$9 million in 2005 and to US$17.6 million in 2007. Withholding tax was insignificant, ranging from zero to below US$0.78 million, even during the copper price boom.

Figure 4.24: Different taxes paid by mining companies



Source: ZRA (2010).[262]

Under private ownership mining company tax was almost non-existent at below US$0.7 million until 2005, compared to US$8.62 million in 1995 before the mines were privatised. The government started gaining notable mining company tax only from 2006, at US$36.34 million that subsequently increased to US$156.73 million in 2007. The higher company taxes in 2006 and 2007 corresponded with the boom in the price of copper. Nonetheless, these values, at the height of the copper price boom, were still considerably lower than mining tax revenue in the early 1990s, especially since these figures are based on nominal rather than real figures.

[262] Information sent on request.

CHAPTER 5

5. THE PRIVATISATION OF THE MINING SECTOR AND THE IMPACT OF CHANGING OWNERSHIP AND MANAGEMENT STRUCTURE ON THE ZAMBIAN ECONOMY

This chapter addresses the research questions as to: (i) the privatisation approach of the government in the mining sector and the development consequences for Zambia; (ii) the changing objectives and management structure under different ownership and the impact on growth and the socio-economic development of the Zambian economy; and (iii) the political-economic implications of the privatisation and private ownership of the mines and the impact on development.

The privatisation process of the mining sector is first considered, followed by an assessment of the regulatory and institutional capacities of the Zambian government in the privatisation of the ZCCM. The role of the privatisation of the ZCCM in improving public finances is then investigated. Subsequently, the changing ownerships and management structure and their impact on mining performance and on the socio-economic development of Zambia are examined. The political-economic implications of the privatisation and the private ownership of the mines and the impact on development are then explored.

5.1 THE PRIVATISATION OF THE MINING SECTOR

This section investigates the privatisation process of the ZCCM and key influences. The main stages in the privatisation of the ZCCM are then reviewed. Further, the bidding process of the Kafue Consortium and of Anglo American and factors influencing the timing of the final assets of the ZCCM are evaluated. This is followed by a brief outline of the main transactions in the privatisation of the ZCCM.

5.1.1 The privatisation process and key influences

As described in earlier chapters, Zambia's international debt and the corresponding influences of the World Bank and the IMF diminished the leverage of the Chiluba government to determine whether it wanted to privatise the mines. Rather, the focus of the Chiluba government was shifted towards 'how' rather than 'why' the copper mines of Zambia were to be privatised. The donors, in turn, in a bid to push the privatisation agenda, bought the MMD an extended political honeymoon, by increasing aid to the Chiluba government in the first few years of its rule. The increases in aid were designed to cushion Zambians against possible difficult social and political consequences likely to arise from the massive and rapid structural changes to the economy. The budget became more than 40% donor-dependent during this time (Fraser & Lungu, 2007:9).

Despite the weak position of the Zambian government, political interference in the process of privatisation strongly marked the privatisation of the ZCCM. The institutional framework established for privatisations, in general, was amended in the case of ZCCM, elaborated upon in Section 5.2, to enable greater political influences in the privatisation process. The options considered in the privatisation of the ZCCM and the decision-making processes are now considered.

Options

The Chiluba government considered three options between 1992 and 1996 for implementing the privatisation of the ZCCM that are briefly outlined below. The influence of the unbundled option that was eventually adopted in the privatisation process of the ZCCM is evaluated in greater detail.

Option 1: A single TNC or a consortium of TNCs acquiring a controlling interest in the ZCCM

This option was rejected as the government feared that the likely control of Anglo American over the ZCCM under this option would have subjected the copper industry of Zambia to the corporate interests of Anglo American. The government was particularly apprehensive that a possible preoccupation of Anglo American with its South African interests and with longer-run projects would likely have encouraged the company to neglect and delay large-scale rehabilitation and the development of the new mines and the mining industry in Zambia (Craig, 2001:393, 394). While this option was rejected, Anglo American continued to exert considerable influence in the process of privatising the mining sector until its departure in 2002.

Option 2: Private ownership and independent operation of the ZCCM

The private and independent option[263] would have entailed the refinancing of and a decrease in government shares in the ZCCM, to convert it into an independent private sector company. Such a privatisation strategy would have circumvented problems associated with dismantling the company and would have prevented the ceding of control to foreign ownership (Craig, 2001:395). The achievement of this option was unlikely, in light of:

- The improbability that the government would have been able to raise the required finance for the future development of the ZCCM and to establish it as an independent private sector company.
- The losses that the company experienced in the 1990s, from 1995 to 1999,[264] and of the declining production levels of the ZCCM (refer to Table A6, in Annexure).
- The extensive rehabilitation of the ZCCM that was required to restore investor confidence and with the poor likelihood that the existing management possessed the necessary skills to do so.
- The possibility that Anglo American would have exercised its pre-emptive rights to prevent the government from selling over 10% of its shares in the ZCCM to the Zambian public and/or to foreign investors (Craig, 2001:396).

Option 3: Unbundling and sale of components of the ZCCM

The option of unbundling the ZCCM, first recommended in June 1994, in the Kienbaum Development Services Report, would have enabled each investor to enjoy majority interest in the 'unbundled' sections of the ZCCM. However, the ZCCM was to retain a role in technical support and services. This option had to overcome the opposition of Anglo American, as minority shareholder and on account of the pre-emptive rights it enjoyed in the ZCCM (entailing also an effective right to veto the sales of the major assets of the company once the government's shares fell below 50%) and through its

[263] Partly inspired by the successful privatisation of the Ashanti Goldfields Company of Ghana.
[264] The ZCCM also experienced losses in the 1993-1994 financial year.

representation on the ZCCM Board of Directors (Craig, 2001:391; Afronet, Citizens for a Better Environment and RAID, 2001:34). The unbundled option was eventually selected as the preferred option for the privatisation of the ZCCM.

The decision-making process

The options and process to be followed in the privatisation of the ZCCM were mainly determined through the deliberations in the reports of advisors to the Zambian government and through the positions of different interests, including the World Bank, Anglo American and the ZCCM management. The ZCCM managers largely acted in the interests of the Zambian government. Two sets of advisors, Kienbaum and Rothschild and Clifford Chance, set out the privatisation of the ZCCM in their reports that are discussed separately below.

(i) The Kienbaum Report

The Kienbaum Report of June 1994 was prepared by Kienbaum Development Services, German advisors, and was funded by the World Bank. The report recommended a rapid privatisation and a division of the assets of the ZCCM into six bundles. The report also recommended imposing a series of commitments on the buyers to ensure continuity in the provisions of social services to the mining communities, which would have been more favourable to the Zambian mining community. Incentives discouraging private companies from rapidly withdrawing from the provision of water, sanitation, health, education and recreational services would have promoted continuity in the provision of social services (ZCCM-IH, 2001:1; Transparency International, 2002:18, 19).

However, Anglo American vigorously opposed the recommendation for unbundling. Reasons that Anglo American cited for its opposition entailed firstly, likely increases in costs owing to a duplication of functions by the different mining companies in their endeavours to become self-sufficient in their mining operations. Secondly, it reckoned that a separation of the blending process would be disruptive to normal mining operations, with each mine being forced to become dependent on other mining units for concentrating, smelting and refining activities (Kaunda, 2002:182).[265] Moreover, selling the ZCCM as a single unit would also have served Anglo American's strategy to enter Zambia's mining industry from a position of strength (Kaunda, 2002:182).

Ultimately, a combination of reasons led to the Zambian government rejecting the report. These reasons included: Anglo American's opposition to the unbundling of the ZCCM; the failure of the report to provide an implementation plan for the unbundling strategy; and an apprehension that a likely collapse of weaker divisions that might have proven difficult to sell through an unbundling process would result in mass redundancies (Kaunda, 2002:31, 32; ZCCM-IH, 2001:1). Allegations that the advisors had leaked information to potential buyers further fuelled the government's opposition to the Kienbaum Report.[266] The Kienbaum consultants were subsequently replaced by the UK-based financial and legal advisors, NM Rothschild and Sons (Merchant Bankers) and Clifford Chance[267] respectively, to continue further studies on the privatisation of the ZCCM (Craig, 2001:395).

(ii) The Rothschild Report

Two years after the government's rejection of the Kienbaum Report, in June 1996, the Rothschild Report came up with similar recommendations in that it also proposed an unbundling of the ZCCM, although it recommended eight separate business packages instead of six. However, the Rothschild Report differed in several other respects to the Kienbaum Report. First, it had a much weaker emphasis on the commitments of the private buyers to the continuity in the provisions of social services to the mining communities and on incentives to discourage private companies from rapidly withdrawing from the provision of water, sanitation, health, education and recreational services. Second, lower government shares, through the Zambia Consolidated Copper Mines-Investments Holdings (ZCCM-IH) that represented the government in the different mining companies, ranging from 10% to 21% (refer to Table A5, in

[265] Interview with Silane Mwenechanya, 24 October 2003.
[266] Interview with Wilphred Katoto, 12 November 2003.
[267] The World Bank sponsored the Kienbaum as well as the Rothschild and Clifford Chance advisors to the government in the privatisation of ZCCM (interview with Stuart Cruickshank, 28 October 2003; Transparency International, 2002:18, World Bank, 2002a:4, Kaunda, 2002:27, 32; Maambo, 1998:Fig. 10).

Annexure), reduced the share of profits retained in Zambia (Transparency International, 2002:1, 2, 18, 19; ZPA, 2000b:15, 2000c:34; Muchimba, 1998:5; ZCCM-IH, 2001:1).

Again, Anglo American possessed strong leverage in being able to influence the recommendations of the Rothschild Report, as these had to be broadly acceptable to ZCI[268] Directors (Craig, 2001:395). Only after Anglo American accepted the unbundling process proposed in the Rothschild Report did the Chiluba government, who previously rejected the proposal for unbundling the ZCCM,[269] accept a similar though more comprehensive proposal for unbundling.[270] An opportunity to acquire and develop the lucrative Konkola Deep[271] from the rest of the ZCCM that the government, through lack of funds, was forced to give up, led to Anglo American subsequently waiving its pre-emptive rights and accepting the unbundling strategy for the ZCCM (Craig, 2001:399).

In order to make the unbundled option that the Rothschild Report proposed even more palatable for Anglo American, it obtained a 5-year management contract of SmelterCo[272] at the close of its transaction, to facilitate its processing activities in an unbundled ZCCM. SmelterCo, together with the Nkana smelter and refinery, was critical to the operations of KCM, as the largest producer of copper in Zambia.[273] Furthermore, Anglo American, through KCM, enjoyed an additional three-year exclusive option to purchase SmelterCo's assets,[274] with a right to refuse bids received in the remaining two years (ZPA, 2000c:39; ZCCM-IH, 2001:3). The exclusive option granted to Anglo American was also deemed necessary to enable the company to evaluate the viability of an alternative long-term metal processing route, through biometallurgical processing technology, within the three years (ZPA, 2000c:39; World Bank, 2003b:133; ZCCM-IH, 2001:1; Kaunda, 2002:96).

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268 Anglo American's subsidiary that had a minority ownership of the mines.
269 Put forward in the Kienbaum Report.
270 Interview with Silane Mwenechanya, 24 October 2003.
271 Described by ex-ZCCM Chief Executive, Francis Kaunda, as "the jewel of ZCCM's crown without which the rest of ZCCM is a dead duck."
272 Chilean experts rehabilitated SmelterCo during the two years that it was under Anglo American's management control, with a £50 million grant from the UK government (ZCI made conditional a requirement for a grant on the closing of their deal that led to the smelter then being operated at profitable levels (interviews with John Lungu, 12 November 2003 and Stuart Cruickshank, 28 October 2003).
273 Interview with Simon Capper, 30 October 2003.
274 MCM enjoyed a second option on SmelterCo's assets (ZCCM-IH, 2001:3).

While Anglo American came to support the unbundling option, due to advantages it held for the company, the Chiluba government's shift towards unbundling was further influenced by a new understanding that this option would play an important role in maximising investment, bringing in expertise and reducing risk. A single investor would probably not have been able to invest the estimated US$3 billion that was required for rehabilitating the mine. A diversity of ownership would also have enabled the participation of varied expertise in the mining industry (Kaunda, 2002:31, 32; Craig, 2002:364). It was also understood that an unbundled ZCCM would minimise the political and economic risks to Zambia, as it would prevent any single company, or consortium, from gaining monopoly control over the industry and an influence over the national economy (ZCCM-IH, 2001:1; Maambo, 1998:Fig. 10; Craig, 2002:364; Kaunda, 2002:31, 32).

5.1.2 Main stages in the privatisation of the ZCCM

The privatisation of the ZCCM was to take place in two stages. This was to enable the company to deal with the huge debt that the ZCCM had accumulated, the social service provisions that formed part of the company's administrative policy and the disposal of non-core assets of the ZCCM, such as houses, hospitals and schools (Transparency International, 2002:1).

Stage one involved the sale of substantial majority interests in the ZCCM's mining, treatment and power distribution operations, offered in separate packages to private investors, with the ZCCM maintaining minority interests. Instead of the scheduled period of 1997, the first stage of the Rothschild and the Clifford Chance recommendations were completed only in March 2000,[275] following the transferral of all productive assets of the ZCCM to private ownership. The residual holdings of the ZCCM were converted into an investment company under the name of the ZCCM Investment Holdings plc (ZCCM-IH) on 21 June 2000 (Craig, 2001:390, 407). Stage two entails the government selling some, or all, of its residual shareholding in the ZCCM to the local and foreign public and to financial institutions (Kaunda, 2002:38;

[275] The finalisation of the terms agreed to in January 1999 until March 2000 was delayed by the stipulation that Anglo American includes at least, one other mining company within the consortium (Craig, 2001:406).

Craig, 2001:397; ZPA, 2000c:34; Muchimba, 1998:5). No timetable was set for stage two of the privatisation of the ZCCM and it had not been addressed by 2009 (ZCCM, 2000:9).

5.1.3 The bidding process of the Kafue Consortium and of Anglo American and factors influencing the timing of the privatisation of ZCCM's final assets

The relative merits of the Kafue Consortium and Anglo American bids and the effects of the delay in the privatisation of the mines are major areas of contention between different parties, such as the World Bank, the Zambian Privatisation Agency (ZPA) and the Privatisation Negotiating Team. The Privatisation Negotiating Team was the body the government established to commence negotiations in the privatisation of the ZCCM. The timing of the sales of the final and most lucrative assets of the ZCCM was closely related to the bargaining over bids received. Especially the bargaining process of the Kafue Consortium, the ultimate rejection of the bids received from the Kafue Consortium and various demands from, in particular, Anglo American that certain conditions be met before the sales of the 'Aco' package were finalised, determined the timing of the sales.

The discussion below first examines the bids of the Kafue Consortium and of the Anglo American Consortium, followed by an evaluation of arguments by some that the delay in the privatisation process enabled Anglo American to substantially lower its bid below that of the Kafue Consortium bid.

Kafue Consortium and the Anglo American bids

The bid of the Kafue Consortium for package 'A' of the ZCCM proposed in September/October 1997 was, in fact, accepted by the government.[276] The bid package, comprising of Nkana/Nchanga (A), Chambishi Acid and Cobalt Plants (G) and the Chingola Refractory Ores (L), amounted to about US$370 million. This matched closely the valuation of US$399 million that the Negotiating Team calculated for the assets of that package. However, subsequently, the Kafue Consortium made further

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[276] The offer that was officially announced on 7 November 1997.

major downward revisions in 1998, which departed significantly from the agreed commercial terms that had formed the basis for finalising the transaction documents of the September/October 1997 offer. The revision led to the Negotiating Team terminating the exclusive negotiations of the Kafue Consortium (Kaunda, 2002:65, 66).

As is illustrated in Table 5.1, the downward revision in the 10 March 1998 bid from the September/October 1997 offer included the demand for more concessions. The concessions entailed tax waivers below what the Negotiating Team was offering and an inclusion of additional assets that were not in the original package. These assets were the Ndola Lime Company (NLC), the Dar-es-Salaam Port facility, the Nampundwe Mine, the bulk transport fleet and the parts manufacturing facility (Transparency International, 2002:22; Kaunda, 2002:66). Moreover, the timing of the 10 March 1998 bid appears to have been deliberate to coincide with the week before the Consultative Group meeting in Paris on aid to Zambia, in which the privatisation of the ZCCM was to feature as a major conditionality (Kaunda, 2002:66).

In a revision released on 31 March/April 1998, the Kafue Consortium further reduced the bid value in a number of areas over the October 1997 bid. Moreover, the claim of the Kafue Consortium that they were to invest US$1 billion in the mines, in their revised offer of June 1997, is also misleading. Calculations performed by Rothschild show that the value of the retained interest of the ZCCM amounted to merely US$90 million over a period of 10 years and that the discounted value of debts to be assumed was only US$42 million. Accordingly, the investment commitment of the Kafue Consortium bid was then brought to US$200 million and the total investment of the revised June 1997 bid to US$492 million; far short of US$1 billion (Kaunda, 2002:62). The Negotiating Team rejected the revision of the Kafue Consortium bid and after a delay of a further two years it reached an agreement with Anglo American in the privatisation of the final assets.

Table 5.1: Comparison of bids made by the Kafue Consortium

October 1997 (accepted by the government)	10 March 1998	31 March/April 1998
• Cash consideration US$150 million • Debt assumption US$75 million • Committed investment US$400 million • Cobalt price participation benefits to the ZCCM of US$75 million • The ZCCM retained interest of 12% (valued at US$70 million) • Less demanding tax adjustments The October 1997 bid amounted to US$370 million, while the ZCCM valuation of the package was US$399 million	• Cash consideration of US$200 million, broken down to US$50 million on closure, with three additional tranches of up to US$50 million each, payable at the end of the second, third and fourth years. The tranches were tied to the average copper price on the LME that was to commence at closure • Debt assumption US$35 million on closure, with a further US$40 million after 5 years, provided that the average LME copper price over the five-year period was 95 cents/pound or 'high' • The ZCCM retained an interest of 12% (but free carry was eliminated) • Demanded the inclusion of the NLC Limited, Nampundwe Mine, the Dar-es-Salaam port facility, the bulk transport fleet and the parts manufacturing facility in the package	• Cash consideration US$105 million, provided that a percentage of the amount was placed in a retention account, pending the resolution of cash adjustments not previously discussed • Among the items for cash adjustment was a demand for 300 houses, in addition to the institutional houses attached to the mining assets in the package; or it was to deduct US$150 000 from the cash consideration, for each house they should have received • Debt assumption US$35 million to be undertaken after 5 years, provided that the LME price of copper did not fall below 95 cents/pound • Committed investment expenditure US$400 million • The ZCCM carried interest was reduced to 6%, all payable

Sources:Kaunda (2002:65-67); Bull (cited in Profit Magazine, 1998:127).

Several pressures that impinged on the Zambian government, especially after the collapse of the Kafue Consortium bid, elaborated in Table A6 (in Annexure), the absence of rival bidders to Anglo American for the Nchanga and Konkola mines,[277] and the low copper prices weakened the government's bargaining leverage during the privatisation of the final assets of the ZCCM. Donor pressure included making the release of US$530 million of balance of payment support, pledged in May 1998, conditional on the completion of the ZCCM's privatisation (Craig, 2001:405). The poor health of the economy, described also in Chapter 4, together with the weak performance of the ZCCM further lowered the bargaining leverage of the government immediately before the mines were privatised. Additionally, inside knowledge of the poor economic position of the ZCCM that Anglo American was privy to, mainly owing to its position as shareholder, strengthened the bargaining power of Anglo American (Craig,

[277] Interviews with John Lungu, 12 November 2003; Dave Phiri, 23 October 2003 and Simon Capper, 30 October 2003.

2001:406).

These pressures encouraged the downward bid of Anglo American and forced the government to accept more flexible and lenient privatisation policies with the company than it had hoped for (Craig, 2001:403, 404, 408). The more lenient policies encompassed a compromise on certain government objectives, such as an acceptance of a lower sale price and increased foreign ownership. Most importantly, Anglo American was able to extract additional concessions from the Zambian government over those received by other mining companies (Craig, 2001:408).[278]

The terms of the sale concluded with Anglo American under ZCI[279] were as follows:

- Cash payment of US$90 million (comprising of an immediate cash payment of US$30 million and of US$60 million, payable in six instalments, starting from 1 January 2006)[280]
- Committed investment for existing operations of US$208 million
- Investment to develop Konkola Deep of US$523 million
- Retained interest for the ZCCM, 20% of equity (5% free:15% carried)

Sources: Africa Research Bulletin (2000a:14302); Craig (2001:406); Kaunda (2002:89); ZCCM (2000:8); ZPA (2000:38).

Evaluation

Insight of the negotiation process in the privatisation of ZCCM reveals the challenges a developing country face in the privatisation of SOEs and the influence of different interests, including major multinational mining houses and foreign donors in the privatisation process. In the mining sector case study the decision of the Zambian Negotiating Team to reject the offer of the Kafue Consortium for the most lucrative assets of the ZCCM was widely criticised by the World Bank and experts in the ZPA. These criticisms are based firstly on the argument that the terms of the Kafue Consortium bid were superior to those subsequently agreed to with Anglo American

[278] Interview with Dave Phiri, 23 October 2003.

[279] The ZCI is a wholly owned subsidiary of Anglo American plc, listed on the London Stock Exchange. Anglo American plc in turn comprises the merger of Minorco S.A. and Anglo American Corporation and Konkola Copper Mines plc and was established to take over the responsibilities of the acquired assets (ZPA, 2000c:150).

[280] Interview with L. M. Lishomwa, 29 October 2003.

that the government, because of various sustained pressures, was forced to accept. Secondly, these experts argue that the two-year delay in the completion of the privatisation process, following the rejection of the Kafue bid, undermined the potential for the recovery of the mining industry. This was mainly due to the deterioration of plant and machinery and because the government was unable to cash in during a period when the copper price was relatively high (Craig, 2002:366).

These arguments are evaluated first, through comparing the Kafue Consortium bid and the Anglo American bids and second, through assessing the effects of the delay in the privatisation of the ZCCM, including its impact on the degradation of the assets of the ZCCM. Third, the policy conclusion of experts at the ZPA and the World Bank that a quick privatisation was to be preferred is evaluated.

1. Assessment of the Kafue Consortium bid and the Anglo American bid

The Kafue Consortium comprised of:

1. Anglovaal Mining Limited (AVMIN), specialists in deep-level mining, from South Africa;
2. Noranda Mining and Exploration Inc, specialists in smelting and refining, from Canada;
3. Phelps Dodge,[281] specialists in open cast mining from the USA; and
4. the CDC, based in the UK, major development financiers throughout the Commonwealth that up to then had contributed much to the success of Zambia's privatisation programme (Bull, cited in Profit Magazine, 1998:126; Kaunda, 2002:58).

The four entities, Anglovaal, CDC, Noranda and Phelps Dodge that previously had pre-qualified individually for the fixed assets of the ZCCM, subsequently formed one consortium at the pre-qualification stage. The broad-based nature of the Kafue Consortium comprising of highly reputable companies with varied expertise and

[281] That was in 1996 the only bidder for the Nchanga and Nkana mines. These mines comprised about 60% of Zambia’s copper production.

business cultures[282] held significant advantages for Zambia. The formation of the consortium raised its capacity to mobilise huge sums of capital to inject into the Zambian mines (Kaunda, 2002:58, 59).

The broad-based ownership of the Kafue Consortium would further have hedged the country against a possible disastrous impact that a withdrawal under sole ownership might have held for the Zambian economy. This is because a withdrawal by one of the members might not always have been followed by other members.[283] A diversification of ownership away from Anglo American, whose shareholders on the London Stock Exchange then opted for a strategy away from Africa, represented a further advantage that a Kafue Consortium takeover of these assets would have held for Zambia.[284] However, the decision to form a consortium and to submit a single bid was probably based less on consolidating resources than on a strategy to reduce competition and to secure assets below market value (Kaunda, 2002:58, 59).

On the other hand, Anglo American formed a consortium with the International Finance Corporation (IFC) arm of the World Bank and the CDC, to bid for and to operate the assets of the ZCCM it acquired under KCM. Anglo American was the major shareholder, owning 65% shares in KCM, through ZCI. The IFC and the CDC each possessed a 7.5% share in KCM (Committee on Economic Affairs and Labour, 2000:48, 49, 114).

A direct comparison of the Kafue bid with the Anglo American bid in the calculations of the World Bank is flawed. This is because it fails to take into account the different composition of the assets on which the Kafue Consortium and those on which Anglo American based their bids and the fact that circumstances had changed. The package on which Anglo American based its bid was smaller than those of the Kafue Consortium (Craig, 2002:366; Kaunda, 2002:80). Furthermore, while it appears that the cash payment and level of committed investment that Anglo American proposed fell far short

282 Interviews with Dave Phiri, 23 October 2003 and Sipho Phiri, 30 October 2003.
283 Interview with Sipho Phiri, 30 October 2003.
284 Interview with Sipho Phiri, 30 October 2003.

of the Kafue Consortium's offer that was rejected the year before by the government, a close examination shows otherwise.

Estimations, calculated by piecing together information provided in the range of sales agreements that matched the bigger package on which the Kafue Consortium based its bids, show very similar values between the Anglo American and the Kafue Consortium bids in terms of proposed investment (cited in Craig, 2002:366-367).[285] Accordingly, despite being unable to attain more for the Nchanga and Nkana assets than the government had hoped, investment commitments of the Kafue Consortium amount to about the same level as the total for the variety of commitments made by Anglo American, AVMIN, First Quantum and Glencore for the same assets (Craig, 2002:366-367). The investment commitments of the Kafue Consortium were US$400 million, over five years.

The head of the Negotiating Team, Francis Kaunda, defends their decision to accept the Anglo American bid, arguing that the Kafue Consortium offer of October 1997 was not substantially superior to the Anglo American offer, despite the drop in metal prices, illustrated in Table 5.2 (Kaunda, 2002:84).[286] It was also comparable to the independent valuation of assets conducted by Arthur Andersen and Mineral Resources Development International (MRDI) in October 1997 of US$399 million, based on discounted cash flows for the bigger package. The bigger package comprised of the Nchanga and Nkana Divisions, Chambishi Acid and Cobalt plants and Nampundwe Mine (Kaunda, 2002:84, 85).[287]

The similar value that the government obtained for the mines to those that the Kafue Consortium offered challenges to some extent the arguments of the World Bank and experts at the ZPA that the delay in the privatisation of the mines adversely affected the eventual price that the government received for the assets of the ZCCM. It further discredits the argument that the Kafue Consortium negotiations were far superior to

[285] Which is most relevant to the future prospects of the industry.
[286] Interviews with Francis Kaunda, 20 October 2003 and Dave Phiri, 23 October 2003.
[287] When the realised consideration for the Chambishi Cobalt and Acid Plants (sold to AVMIN) are taken into account.

those of Anglo American (World Bank, 2003b:133; The Economist Intelligence Unit, 2008b:17). In addition, as the Kafue Consortium would have acquired assets accounting for an even greater share of the current production than that of KCM, the Zambian government would likely have been more vulnerable had the Kafue Consortium experienced problems similar to those of Anglo American (Craig, 2002:367).

Table 5.2: Different offers of Aco's assets by the Kafue Consortium and ZCI

Components of bid	Kafue	ZCI
Cash at close	US$131 million (101million if houses were excluded)	US$72 million
Cobalt price participation	No value	US$44 million
The ZCCM retained interest	US$64 million	US$138 million
Subtotal	US$195 million	US$304 million
	The ZCCM's participation was contribution to the Konkola Division assets for a minority shareholding in the new company	The ZCI-led Konkola Deep Mining Project (KDMP) consortium was to provide the required capital for developing the KDMP, estimated at US$720 million
Debt assumption	US$35 million	No debt, since most of the debts were already paid by the ZCCM
Unconditional investment	US$400 million spread over 5 years	US$300 million spread over 3 years

Source: Kaunda (2002:84).

2. Impact of the delay in the privatisation of the ZCCM

The second argument of the World Bank and experts at the ZPA is that the two-year delay in the privatisation of the major operations undermined the potential for recovery of the mining industry. The deterioration of plant and machinery and because the government was unable to cash in on periods when the copper price was relatively high, while the ZCCM continued to build up debt during the delay, undermined the potential for recovery (see, for example, World Bank, 2002b:7, 16). However, the delay was not merely owing to the government's actions and was to some extent necessary.

Various demands from, in particular, Anglo American, that certain conditions be met before the sales of the 'Aco' package were finalised and because of administrative and legal issues that the government had to address with prospective buyers of the mines also significantly influenced the delay.[288] The high leverage that Anglo American possessed in influencing the conclusion for the sales of the mines underscores the poor bargaining capacity of the government in determining the privatisation process (Kaunda, 2002:32, 33). In addition to the differences in the bids, the required administrative processes, and the bargaining power of Anglo American, another reason for the delay was the consideration of the government to first float 10% of government shares in the ZCCM to the public. It was deemed that this might smooth over negative public perceptions linked to the many job losses as a result of the privatisation process (Kaunda, 2002:32, 33).

Some have also alleged that the delays during the Kafue Consortium negotiations for the remaining major assets of the ZCCM[289] were also deliberately orchestrated to prolong the timeframe to obtain large salaries for those involved in the sale of the mines. The delay also facilitated the stripping of more cobalt and copper assets, through corrupt transactions with buyers at the time, possibly also by the ZCCM managers, who faced an uncertain future (ZAM, cited in Committee on Economic Affairs and Labour, 2000:51).[290]

The argument that the delay promoted the considerable physical deterioration of the mining and processing assets of the ZCCM and that it adversely affected production has merit. This is because an earlier inflow of investment would have improved the resilience of the ZCCM to a downturn in the copper price, which would to some degree have lessened the decline in the value of the mines.[291] A more timely inflow of investment would further have promoted an earlier reduction in the costs of production

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[288] These include the raising of finance to settle debts to trade creditors; to pay retrenchments; to fund capital expenditure of the managed assets; to address the issues of the future provision of social services that was part of the responsibility of the ZCCM; to work out the modalities of asset disposal; financing environmental clean-up obligations for potential third party claims; and to keep the ZCCM operational during the privatisation process (Kaunda, 2002:94 and Transparency International, 2002:26).
[289] The Nchanga and Nkana major mining assets.
[290] Interviews with John Kangwa, 21 November 2003 and Fred M'muembe, 14 October 2003.
[291] Interview with Honourable Captain Moono, 2 December 2003.

of the ZCCM (Craig, 2002:366). Also, when the delay advances the timeframe for corrupt practices,[292] which would have a very negative impact on the economy, then privatisation has to be done swiftly, according to the Resident Representative of the World Bank.[293]

However, the large-scale corruption[294] and the deterioration of mining assets were also due to a wider framework than the delay in privatisation. The absence of effective institutions and enforcement mechanisms to curb corruption at the time the ZCCM was privatised also facilitated corrupt practices. The policy of the IMF and the World Bank that barred the government from reinvesting into the mines tranched for privatisation and to withhold donor balance of payment support until the ZCCM was privatised, was also greatly responsible for the consequent lack of reinvestment into the mines. The lack of reinvestment contributed, most significantly, to the degradation of the assets of the ZCCM, which, in turn, propounded the poor economic performance of the ZCCM.

Irrespective of the delay, reinvestment into the mines and more effective and strong institutions before privatisation policies were implemented, would have limited the degradation of the assets of the ZCCM, the subsequent losses the company incurred and the corruption, which allegedly transpired during the privatisation of the ZCCM. These measures would also have enabled a smoother privatisation of the mining sector. In the absence of reinvestment into the mining sector and of effective institutions, the delays merely propounded but did not initiate the corruption and the degrading of the mining assets. Instead of barring reinvestment into the mines earmarked for privatisation, investment of new equipment into the mines before privatisation that would likely have contributed towards a better performance of the ZCCM could merely have been factored into the price of the mines.[295] A slower pace of privatisation, to allow for appropriate institutional building and of enforcement measures to facilitate a smoother privatisation process and for a less severe impact of privatisation on mineworkers, the Zambian community and on the economy, might, in fact, have been more beneficial.

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[292] Interviews with Ohene Nyanin, 29 November 2003 and Fred M'muembe, 14 October 2003.
[293] Interview with Ohene Nyanin, 29 November 2003.
[294] Interview with Fred M'muembe, 14 October 2003.
[295] Interview with Zion Simwanza, 1 December 2003.

Furthermore, the argument that the drop in copper prices played a significant role in lowering the Anglo American bid is exaggerated. This is because the decline in the price of copper was most severe from the beginning of 1997 to early in 1998, corresponding with the period of the Kafue Consortium's negotiations, and which continued on a downward trend for another year. However, the level reached in 2001 was not much lower than those of early 1999 (Craig, 2002:367).

As such, any agreement that would have been reached with the Kafue Consortium might have run into problems similar to those experienced by Anglo American (Craig, 2002:367). Moreover, the price of copper is independent of delays and while it incidentally declined during the delays, an increase in the price could also have been possible, in which case the delay would have had a positive impact on the sale price of the mines. The argument of the World Bank that the possibility of price declines would lower the asset value of the resource sector cannot, therefore, be a precept for a quick privatisation.

The blame that the World Bank and some experts at the ZPA place on the delay in the privatisation of the ZCCM and the policy prescription for a swift privatisation of state assets to circumvent uncertainties that might arise from delays in the privatisation process is therefore misplaced. Rather than the delay per se, which might not necessarily have yielded a negative impact on Zambia's development under different contextual realities, other factors influencing the mining sector during the delay were responsible for its poor performance. Opportunistic practices were, in fact, encouraged by the rushed processes, predominantly due to pressure from the IMF, the World Bank and other donors.[296]

Instead of the rapid privatisation that neo-classical theorists favour, the pace, sequencing and scope of privatisation seem important for a more orderly restructuring. Effective legal and institutional structures are crucial for promoting successful

[296] Interviews with Willie Sweta, 30 October 2003; M. Shandavu, 10 October 2003 and John Lungu, 12 November 2003.

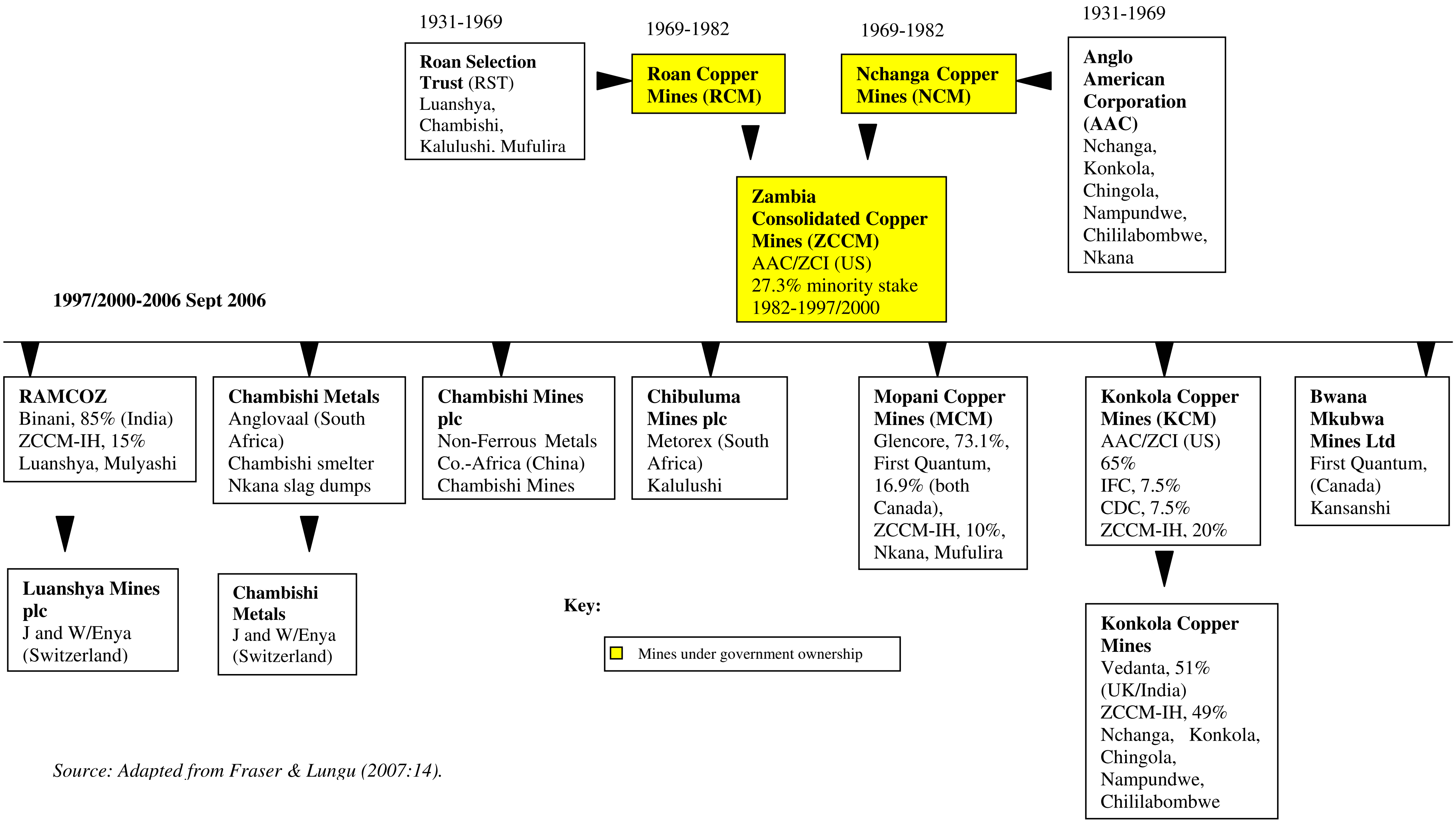
privatisation. A too rapid privatisation or ‘shock therapy’ that radical market reformers favour would also likely carry political costs that would hinder further reforms (Stiglitz, 1998:19, 22).

A gradual approach enables better designs and sequencing of reform and the creation of requisites for good privatisation; including the creation of more effective institutions. A gradual approach would also provide the privatisation with greater legitimacy that would likely ensure more successful outcomes from the privatisation process (Stiglitz, 1998:19, 22; 2002:162, 182, 183-184). The speed of privatisation needs to be balanced against clear long-term legal rules and against a transfer process that is considered as legitimate by the population (Rose-Ackerman, 1999:44). The weak legislative processes in Zambia (elaborated on in Section 6.5.1.6 of Chapter 6) also facilitated, by 2002, the exit from the mining sector of three of the seven major private mining companies that took over ownership of the mines, discussed below.

5.1.4 Main transactions in the privatisation of the ZCCM

Table A5 (in Annexure) provides a summary of the principal terms of sales of the various companies for the different assets of the ZCCM and the main transactions involved in the privatisation of the ZCCM. Kansanshi, the first asset of the ZCCM, was privatised in January 1997 and the remaining major assets of the ZCCM, sold to KCM and MCM, were only finalised on 31 March 2000. Several material changes took place in the control and ownership of the main copper mining assets in Zambia since the privatisation transactions were completed. This is because shares and shareholding companies change hands rapidly and the ownership structures of all the companies are still fairly fluid (Craig, 2002:368). Figure 5.1 shows the different assets held first by the different private companies, then under government majority ownership and again under private ownership, in chronological order.

Figure 5.1: Shifting ownership patterns for large-scale copper mining assets in Zambia from colonialism to 2007



Source: Adapted from Fraser & Lungu (2007:14).

The mining TNCs that exited from Zambia were first Binani that owned majority interests in RAMCOZ at the Luanshya/Baluba mines (that was put under receivership in November 2000), followed by AVMIN, the majority owner of Chambishi Metals. The departure of Binani led to the Luanshya/Baluba mines lying idle for three years, before they were acquired, in 2004, by J and W, a subsidiary of the Swiss company, Enya, that also took over the mines owned by AVMIN (Fraser & Lungu, 2007:13). Moreover, Anglo American pulled out from KCM in 2002, after operating KCM for almost two years (The Economist Intelligence Unit, 2007b:35). Subsequently, Vedanta Resources took over KCM in 2004.

5.2 ASSESSMENT OF THE REGULATORY AND INSTITUTIONAL CAPACITIES OF THE GOVERNMENT IN THE PRIVATISATION OF THE ZCCM

Various theoretical arguments, discussed in Chapter 3, favour the establishment of a robust legal and institutional framework before privatisation is introduced to ensure more favourable outcomes for the country from privatisation and under private ownership. Broadly, a robust legal and institutional framework is essential mainly to curb possible pitfalls, such as corruption and negative influences that might arise during the privatisation of SOEs and under private ownership. Kenneth Arrow's groundbreaking work on the dynamics of why and when market economies work and how economies change regards the creation of institutional infrastructure, together with competition, as more important than privatisation itself for a market economy (Stiglitz, 2002:182).

The assessment of the regulatory and institutional capacities of the government in the privatisation of the ZCCM encompasses an investigation of the supporting institutions and the legal framework established for the privatisation of the ZCCM. Secondly, weaknesses in the legal and the institutional framework evident in the privatisation of the ZCCM are examined.

5.2.1 Supporting institutions and legal framework for the privatisation of the ZCCM

The Privatisation Act of 1992 sets out the legal framework for the privatisation of SOEs. This Act authorised the creation of the ZPA as the most important supporting statutory body provided with the mandate to undertake all the privatisations in Zambia.[297] The ZPA is an independent body with a 12-member board. Nine of these members (including the Vice Chairman) are non-government nominees from the professional institutions and stakeholders they represent (as required by legislation) and only three are government representatives. The private bodies represented on the board of the ZPA are the trade unions, the Churches of Zambia, the Chambers of Commerce and Industry, the Banks Association of Zambia, the Zambian Institute of Chartered Accountants, the Law Association of Zambia, employers, farmers and the Dean of the Business School at the University of the Copperbelt (Afronet *et al*., 2001:11, 12).[298]

The ZPA reports to Parliament via the National Assembly. Information from the ZPA is conveyed to the Cabinet through the Minister of Commerce, Trade and Industry who in turn reports to the National Assembly.[299] The ZPA is generally observed to have well-functioning procedures and governance structures (Craig, 2002:5; Transparency International, 2002:7, 9; Momba, 1998/1999:8).

Section 32 (1) of the Privatisation Act makes a clear distinction between the role of the government and that of the ZPA. This section legally empowers the ZPA as the sole body in charge of all sales transactions, the closure of each sale and in conducting the privatisation process, including the planning, managing, implementing and the controlling of divestiture of SOEs. These were to be free of political interference (Committee of Public Investment, cited in Afronet *et al*., 2001:15; Transparency International, 2002:8, 13).

The Privatisation Act also empowers the ZPA board and not the President to appoint an

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297 Interviews with Valentine Chitalu, 22 October 2003; Stuart Cruickshank, 28 October 2003 and M. Shandavu, 10 October 2003.

298 Although the President has to agree to each of the appointees selected by the independent bodies (Craig, 2002:5, 6; Transparency International, 2002:9 and interview with Simon Capper, 30 October 2003).

299 Interview with Stuart Cruickshank, 28 October 2003.

independent body in instances where additional technical expertise is required. This was the case with the privatisation of the non-mining assets of Zambia (ZPA, 2003:2, 5; Transparency International, 2002:14, 17).[300] The Act confines the role of the government mainly to an advisory position to the ZPA and the government was also to determine the overall direction and timing of privatisation (World Bank, 2002b:15; ZPA, 2003:4, 6).

The government undertook a comprehensive review of the laws, regulations and administrative measures affecting the mining industry. The review culminated in the enactment of the Mining Policy and the Mines and Minerals Act in July 1995 that, together with the provision of incentives to attract and promote private investments in the mining sector, were favourable to private sector investment (Ministry of Finance and Economic Development, 1995:58; Ministry of Mines and Mineral Development, 2003:2). Further legislation to support the privatisation process includes the Investment Act, the Employment Act, the Companies Act and the Securities Act (Transparency International, 2002:7).

5.2.2 Weaknesses in the legal and institutional framework in the privatisation of the ZCCM

The ZPA had undertaken several privatisations of non-mining interests before that of the ZCCM. However, during the privatisation of the mining sector the Chiluba government introduced substantial changes to the procedures for the privatisation of the ZCCM.[301] These changes allowed for the introduction of political interests into the privatisation process and promoted irregularities and non-transparency in the management of the proceeds from the sales of the ZCCM. Regulatory measures to protect the interests of the mineworkers and the mining community against the impact of privatisation were also inadequate. These changes are now examined in greater detail.

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[300] Interviews with Honourable Dipak Patel, 15 October 2003; Silane Mwenechanya, 24 October 2003; Stuart Cruickshank, 28 October 2003; Dennis Wood, 21 October 2003; Danny Kalyalya, 31 October 2003 and David Chilipamushi, 20 October 2003.

[301] Interviews with Valentine Chitalu, 22 October 2003 and Stuart Cruickshank, 28 October 2003.

The introduction of political interests

The introduction of political interests in the privatisation of the ZCCM was largely achieved through the Chiluba government setting up a parallel body to the ZPA, the Privatisation Negotiating Team, to lead the privatisation process and to complete the rest of the privatisations of the ZCCM.[302] Francis Kaunda, former Chairman and CEO of the ZCCM assumed chairmanship of the Negotiating Team that comprised also of various Zambian experts, including several senior employees of the ZCCM, who possessed considerable knowledge of the mining industry (World Bank, 2002b:15). The Negotiating Team, whose creation the World Bank sanctioned, effectively subverted and usurped the roles of the ZPA (Afronet *et al*., 2001:11, 12).

The politicisation of the Negotiating Team included its having to report to the Committee of seven Ministers (chaired by the Ministry of Mines and Mineral Development) to make recommendations for approval, before further approval was sought from the ZPA board and the ZCCM board of Directors. The approval of these bodies was necessary to legalise the privatisation decisions.[303] The inclusion of several senior employees of the ZCCM within the Negotiating Team to negotiate the sales of the ZCCM, many of whom were opposed to the privatisation of the ZCCM,[304] introduced further vested interests in the privatisation of the ZCCM (Afronet *et al*., 2001:11, 12; Committee of Economic Affairs and Labour, 2000:26, 37, 110; World Bank, 2002b:15, 22).

A lessening of civil society participation in the privatisation process, from mid-1998, through the exclusion of several civil society board members[305] from the ZPA board further facilitated the introduction of political influence in the privatisation of the ZCCM.[306] The limit on the participation of the local society enabled the privatisation of the ZCCM to be steered to a particular agenda and reduced transparency in the

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302 Interviews with Valentine Chitalu, 22 October 2003 and Stuart Cruickshank, 28 October 2003.

303 Interviews with Alick Lungu, 14 October 2003; Fred M'muembe, 14 October 2003; Francis Kaunda, 20 October 2003; Zion Simwanza, December 2003; David Chilipamushi, 20 October 2003; Sipho Phiri, 30 October 2003; Stuart Cruickshank, 28 October 2003 and Silane Mwenechanya, 24 October 2003.

304 Interview with Stuart Cruickshank, 28 October 2003.

305 Namely, the Law Association of Zambia, the Banks Association of Zambia, the Zambian Institute of Chartered Accountants and the Churches of Zambia.

306 Interview with Simon Capper, 30 October 2003.

privatisation of the mining assets (Afronet *et al*., 2001:11, 12). Corruption is likely to grow with the lowering of civil society participation, as their participation is an important element in curbing corruption (Rose-Ackerman, 1997:44-45).

Greater government influence might to some extent have been desirable in the privatisation of the mining sector for ensuring that the greatest share of the rent element from mining accrues to the country and in light of its strategic importance to the Zambian economy. However, the political influence introduced in the privatisation of the ZCCM, without effective checks and balances, increased the discretionary power of the Chiluba government. The higher discretionary power of the Chiluba government led to many decisions related to privatisation such as tender procedures and the distribution of resources, being made at State House. This, alongside weakened institutions, promoted alleged corruption by senior officials during Chiluba's government.[307]

Rose-Ackerman (1997:39) cautions against the involvement of top government officials in the allocation of large contracts, as the fewer restraints these officials enjoy would likely lead to massive-scale corruption. The secrecy that clouded some of the negotiations between the Negotiating Team and the bidders of the mines in the privatisation process further obscured accountability. This fuelled speculation that corruption, or the siphoning off of public funds, allegedly by top government officials, also played a part during the privatisation of the mining sector (Transparency International, 2002:i, 1).

Despite claims that a chain of approval was sought for bids that the Negotiating Team recommended, before actual negotiations commenced with the recommended buyer, the Committee of Ministers that reported to the President effectively selected the bidders and conducted the bidding process (Kaunda, 2002:40).[308] The various levels of agreements from the ZPA to approve the commencement of negotiations with bidders and for the sale of all privatised units in Zambia that the Privatisation Act necessitates were, at times, obtained only after negotiations were completed and presented as a fait

[307] Interviews with the Honourable Captain Moono, 2 December 2003 and Nchima Nchito, 2 November 2003.
[308] Interviews with Zion Simwanza, December 2003 and M. Shandavu, 10 October 2003.

accompli.[309] The boards of the ZCCM and the ZPA were also merely informed of the decisions that the Committee of Ministers already made (Transparency International, 2002:12; ZPA, 2003:2, 4). The ZPA was expected to rubber-stamp decisions already taken by the Committee of Ministers and the Negotiating Team, sometimes setting the Negotiating Team at odds with the ZPA (ZPA, 2003:2, 4, 6).[310]

A weakness within Section 9 (3) of the Privatisation Act itself, which provides for the calling of meetings of the board without the necessary 14 days' notice, in matters deemed urgent, and the stipulation that only five members form a quorum, also assisted in promoting political interests in the privatisation of the mines. This is because, provided that all three Lusaka-based government members were present, these provisions enabled the government to automatically end up with a majority if a meeting was called at short notice. This was the case with the first sale of the Luanshya/Baluba mine (Transparency International, 2002:13). Moreover, since three members of the Negotiating Team, the Attorney General, the Secretary of the Treasury at the Ministry of Finance and National Planning and the Permanent Secretary of the Ministry of Commerce, Trade and Industry, were also sitting on the board of the ZPA, once government approval was granted, the approval of the ZPA became inevitable.[311]

The most prominent example of political interference and possible corrupt practices in the bidding process were allegedly the Negotiating Team's selection of Binani, a copper trader and smelting company with no track record in deep level mining, over First Quantum to acquire the assets of the Luanshya/Baluba mine.[312] The Luanshya/Baluba mine is a deep level mine that is difficult to operate on account of its complicated geology (Africa Mining Intelligence, 2001c:2). The ZPA was excluded from the opening of negotiations with Binani in the Luanshya/Baluba bid and the Negotiating Team refused to comply with the advice of the ZPA to turn down the Binani bid (ZPA,

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309 Interviews with Stuart Cruickshank, 28 October 2003; Dennis Wood, 21 October 2003; Honourable Dipak Patel, 15 October 2003 and M.Shandavu, 10 October 2003.

310 Interviews with Silane Mwenechanya, 24 October 2003; Fred M'muembe, 14 October 2003; Simon Capper, 30 October 2003 and M. Shandavu, 10 October 2003.

311 Interview with M. Shandavu, 10 October 2003.

312 Interviews with Ladslous Mwansa, 7 October 2003; Sipho Phiri and Simon Capper, 30 October 2003; Stuart Cruickshank, 28 October 2003; John Kangwa, 21 November 2003; M. Shandavu, 10 October 2003; Valentine Chitalu, 22 October 2003 and Alick Lungu, 14 October 2003.

2003:2, 6).[313] Ultimately, Binani was wound up in 2000 and the bid was subsequently awarded to J and W, instead of to AVMIN, under the Mwanawasa government, also amidst allegations of political influence (Africa Analysis, 2003a:16).

However, arguments in favour of Binani were their commitments to retain the total workforce at Luanshya/Baluba and to make further investments. Moreover, the Financial and Legal Advisors, Rothschild and Clifford Chance, also participated in the selection of the Binani Group for acquiring the Luanshya mine.[314] It has further been claimed that the ZPA was never forced to rubber-stamp bids that it did not favour.[315] However, the point is rather that under the Chiluba government the whole process was politicised to a much greater extent, enabled through the weak institutions and the fast pace of privatisation pushed for by the World Bank.

Institutional and policy changes that promoted irregularities and non-transparency in the management of the proceeds from the sales of the ZCCM

In addition to the introduction of political influence in the privatisation of the mining sector, the proceeds from the sales of the ZCCM were managed in an irregular and non-transparent way. These were at odds with the structures that the ZPA established to promote transparency and accountability that featured strongly in the privatisation of non-mining SOEs. Transparency and accountability in the privatisation of non-mining assets were mainly achieved through effective communication with the public and also through progress reports that had to be gazetted.

The irregular and non-transparent ways the proceeds from the sales of the ZCCM were managed arose as a result of:

- The failure of the Ministry of Finance and Economic Development that was in charge of receiving and depositing the proceeds of privatisation from the ZPA into the Privatisation Revenue Account (PRA) at the Central Bank to follow proper accounting procedures.

[313] Based on an argument that ZPA could not change decisions made by the Committee of Ministers (interview with Stuart Cruickshank, 28 October 2003).
[314] Interview with Willie Sweta, 30 October 2003.
[315] Interview with Simon Capper, 30 October 2003.

- Discrepancies in the keeping of proceeds from the sales of the ZCCM's assets between accounts of senior officials of the ZPA and those of the ZCCM board.[316] The discrepancies were partly owing to a practice of the Negotiating Team to, at times, deposit the proceeds[317] into a ZCCM account,[318] ostensibly to be used in the operations of the company and for meeting the company's expenses, rather than into the PRA, despite its being a requirement of the Privatisation Act.
- The failure of the Negotiating Team to publish in the government gazette details of the original values of the mining enterprises and of the completed sales and spending figures (which hindered objective assessment as to whether a fair price was obtained for the mines) and to provide a complete list of all the assets of the ZCCM.[319] Besides the inability of the Negotiating Team, the ZCCM and the Ministry of Mines and Mineral Development to verify the price, they were also unable to verify to whom some of these assets were sold and the payment terms.[320]
- A lack of public communication in the privatisation of the ZCCM as to why certain decisions were taken, why Zambia's privatisation took place and as to the processes and the results of privatisation, which is required in the structures of the ZPA. The omission contributed significantly to a less transparent privatisation of the ZCCM, according to a review that the World Bank conducted.
- The non-disclosures of the amount of money that went into the PRA account[321] and of withdrawals from deposits[322] in the PRA account and of the purposes for which these were to be used, making accounting difficult and leading to significant discrepancies in the proceeds obtained from the privatisation of the ZCCM. A shortfall of ZK3 963 822 387 and US$16 824 579 was expatriated from the amount remitted to the PRA. Structures within the ZPA subject each of the sales transactions to the approval of both the Attorney General and the Minister of Finance.
- The failure to publish the public flotation of the remaining shares of the Zambian

[316] ZPA maintained that proceeds were kept in a ZCCM account, while the ZCCM board maintained that proceeds were kept in a government account.
[317] Especially from the sale of some core and non-core assets.
[318] Without any explanations as to the whereabouts of the money.
[319] Despite the Committee on Economic Affairs and Labour requesting these from the Negotiating Team, the ZCCM and the Ministry of Mines and Mineral Development.
[320] Including where it was paid.
[321] This practice, however, happened already at the end of 1995, before the privatisation of ZCCM's assets.
[322] Which are listed in the ZPA Progress Report.

government,[323] making it difficult to verify whether the money generated was deposited in the PRA, as is required by the Privatisation Act.

- The transferring of a number of non-core assets to Trusts and disposing of some by 'deed of gift', which are not provided for in the Act.
- The Negotiating Team's selling especially the non-core mining assets and the ZCCM's overseas assets, without the prior authorisation of the ZPA board, and which, under the 'rules for the implementation and approval of the terms of sale', require the Attorney General's review of the sale agreements and the signature of the Ministry of Finance and Economic Development.
- The employment of confidentiality clauses in the privatisation of the ZCCM,[324] which obscured transparency and impeded detection of possible corrupt practices.

Sources: Afronet et al. (2001:14, 15); Committee of Economic Affairs and Labour (2000:15, 38, 76, 77, 112, 113); Craig (2002:6); Transparency International (2002:5, 13, 14, 15); World Bank (2002b:21); ZPA (2002:5) and interviews with Andrew Sardanis, 19 October 2003; Dennis Wood, 21 October 2003; Fred M'muembe, 14 October 2003; Francis Kaunda, 20 October 2003 and Ohene Nyanin, 29 November 2003.

Together, these weaknesses in the management of the proceeds from the sales of the ZCCM promoted corruption, allegedly committed by senior government officials, at a great cost to the Zambian economy (World Bank, 2002b:15, 21, 30; Transparency International, 2002:i, 1, 7). It is alleged that ex-President Chiluba misappropriated about R1 billion, according to a petition calling for his arrest, and a civil prosecution in a British court in May 2007 found Chiluba guilty of defrauding Zambia of US$46 million, via a UK bank account (The Economist Intelligence Unit, 2007b:10; The Star, 2002b:4). The alleged large-scale corruption corroborates to some extent Rose-Ackerman's (1997:39) argument that when top government officials are involved in the allocation of contracts, massive scale corruption with far-reaching consequences is likely to take place. It also supports the argument of Stiglitz that when effective legal infrastructure to ensure good governance is absent, asset stripping by insiders and the local government is likely to take place (Stiglitz, 2002:144, 155, 157, 158).

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[323] Which can generate significant amounts.

[324] Based on the argument that rules governing shares traded on both the London and New York Stock Exchange prohibit the release of development agreements or documents to outside institutions.

Predictably, the head of the Negotiating Team, Francis Kaunda, contests the allegations of corruption during the privatisation of the ZCCM. He argues that the involvement of many parties, namely the board members of the ZCCM, the B-Directors (represented by shareholders) and the ZPA, required to approve the sales transactions of the mines, reduced the chances of corruption.[325] Francis Kaunda further claims that it was only where individual decisions were made or when too many discretionary powers were provided to certain government officials (possibly the top government officials) that detection of corrupt practices became difficult and that corruption proved likely.[326] However, the argument that the participation of various bodies in the privatisation of the ZCCM lowered the chances of corruption was somewhat discredited by the fact that the various levels of agreements to approve commencement of negotiations with bidders were not always sought in the privatisation of the ZCCM, as discussed above. The ZPA was essentially expected to rubber-stamp decisions already taken by the Negotiating Team and the Committee of Ministers.

Measures to curb corruption in the privatisation process should have been established before the privatisation process commenced, rather than after the corruption took place. For instance, the Task Force to investigate corrupt practices, including the tracking down of illegally sold government assets, was established after large-scale corruption had already transpired, also in the mining sector, during the privatisation process.[327] Furthermore, the independence of the Task Force was compromised because it was commissioned by the Mwanawasa government, a measure that probably excluded that government from the investigation.[328]

Weaknesses in the regulatory framework to protect the interests of the mineworkers and the mining community against the impact of privatisation

Several legislative and institutional weaknesses existed in the protection of workers against adverse consequences arising from the privatisation of the mines.

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325 Interview with Francis Kaunda, 20 October 2003.
326 Interviews with Francis Kaunda, 20 October 2003 and Valentine Chitalu, 22 October 2003.
327 Interview with Dennis Wood, 21 October 2003.
328 Interview with John Lungu, 12 November 2003.

- *The absence of alternative employment*

The Chiluba government failed to create new employment to absorb the many Zambian mineworkers that lost their jobs through privatisation and through trade liberalisation (Stiglitz, 2002:183-184).[329] This is in contrast to China where new jobs were created in tandem with privatisation, which prevented massive unemployment and accounted for the rather successful privatisation of the SOEs in that country. Approximately 29 200 mineworkers lost their jobs in Zambia from 1994 to 2000. About 3 500 mineworkers were retrenched from 1994 to 1996 and most mineworkers, 25 700, lost their jobs from 1996, a year before the first mines were privatised, until 2000 when the last mines were privatised.

Land was provided for agricultural farming through the Kanakatapa Resettlement Scheme as a social cushioning measure to some retrenched workers.[330] However, most retrenchees in Zambia went into subsistence farming, mainly on land owned by the copper mines.[331] Measures to relocate retrenched workers from the ZCCM to agricultural land where they could enjoy title deeds to participate in the agricultural sector seem necessary.

- *Inadequate social security safety nets*

The social security system in Zambia was highly inadequate in taking care of the many retrenched employees (ZPA, 2000b:16).[332] This contrasts with the social safety nets in the form of social programmes provided to retrenched workers in countries of the Organisation of Economic Cooperation and Development (OECD), to soften the negative impact of trade liberalisation. The social safety nets extended to the retrenched workers in these countries included unemployment compensation, insurance, pension, family benefits and adjustment assistance (Rodrik, 1997:23-25).

An effective social security safety net programme and government policies to reduce the negative socio-economic effects of the privatisation of the ZCCM on the Zambian

[329] Interview with Silane Mwenechanya, 24 October 2003.
[330] Interview with Ladslous Mwansa, 7 October 2003.
[331] Interview with John Lungu, 12 November 2003.
[332] Interview with John Kangwa, 21 November 2003.

nation,[333] which was to be sponsored from part of the proceeds of privatisation, never materialised. The omission was partly attributable to insufficient net capital obtained from the proceeds of privatisation.[334] Inefficiencies at the division of the ZPA dealing with the social impact of privatisation[335] and the tight budget constraints of the government, which contributed towards thousands of former workers of the ZCCM not being paid their pensions by 2007, also contributed to the inadequate social security nets provided to mineworkers (Fraser & Lungu, 2007:3).

Furthermore, the attachment of other assets that workers gained during the privatisation process to their retrenchment and pension packages significantly reduced these packages of mineworkers. Houses sold to workers, personal to holder vehicles and loans were attached to their retrenchment packages and the value of the houses were also subtracted from their pensions during the privatisation of the ZCCM. Accordingly, the safety nets provided to those left unemployed were absent or highly inadequate to assist workers and communities that depended on the mines to sustain themselves economically and to cope with the financial difficulties that arose as a result of the privatisation of the ZCCM (Lungu, 2001:6; Fraser & Lungu, 2007:30, 51).

The inadequate safety nets provided to workers had severe adverse repercussions on the mining community and greatly contributed to increased poverty levels in Zambia, discussed in Section 4.4.5 of Chapter 4 (Fraser & Lungu, 2007:5; Lungu, 2001:16, 17; Gostner, 1997:60). The failure to protect those negatively affected by the privatisation process stands in stark contrast to measures that Poland introduced to lessen the impact of privatisation on the broader society. These measures encompassed benefits to the unemployed and adjustments to pensions and salaries in line with inflation, which significantly accounted for Poland's market economy functioning better than those of other East European countries (Stiglitz, 2002:181, 262).

The failure of the government to create alternative employment to accommodate

[333] Interviews with Silane Mwenechanya, 24 October 2003; Wilphred Katoto, 12 November 2003; Charles Muchimba, 18 November 2003; Jack Jones, 22 October 2003; John Kangwa, 21 November 2003 and Fortune Kamusaki, 25 November 2003.
[334] Interviews with Willie Sweta, 30 October 2003 and Valentine Chitalu, 22 October 2003.
[335] Interview with Fortune Kamusaki, 25 November 2003.

workers left unemployed and to introduce effective social safety nets to unemployed mineworkers constituted major weaknesses in the protection of mineworkers during the privatisation process of the mines. Omissions in government policies that affect workers adversely under private ownership of the mines by TNCs are discussed in Section 6.5.1.4 of Chapter 6. Inadequate monitoring and poor enforcement of regulations during the privatisation of the mines and of the operations of mining TNCs further facilitated corruption and reduced more favourable results from the privatisation of the mining sector for the Zambian nation.

Summary

From the above discussion it is noted that the institutional and policy changes that the Chiluba government introduced in the privatisation of the mining sector, from those established during the privatisation of the non-mining assets, precluded a more successful privatisation of the mines in Zambia. These included: (i) the introduction of political interests into the privatisation process; (ii) irregularities and non-transparency in the ways in which the proceeds from the sales of the ZCCM were managed; and (iii) insufficient protection of mineworkers (Transparency International, 2002:17). Poor enforcement also limited the success of the privatisation of the ZCCM.

The alterations in the procedures failed to match the elaborate legal and administrative framework and the procedures and controls that the ZPA followed during the privatisation of non-mining assets to ensure accountability and transparency and to control corruption and mismanagement in the privatisation process (Transparency International, 2002:17). Indeed, the political influence and increases in the discretionary power of the Chiluba government that the changes introduced in the privatisation of the mining sector compromised the independent functioning of the ZPA. These undermined and weakened institution building.

Instead of promoting positive outcomes for the Zambian economy, an over-rapid privatisation, the ‘shock therapy’ favoured by radical market reformers,[336] without

[336] Such as the IMF and the World Bank.

effective legal and institutional structures in place, and with insufficient regard for the policy's social and distributional consequences, facilitated the poor outcomes from privatisation. The poor governance and irregular and non-transparent ways in which the proceeds from the sales of the ZCCM were managed and an inadequate protection of the interests of mineworkers as a result of these omissions facilitated corruption and limited the redistribution of benefits of the privatisation process. Accordingly, the manner in which the privatisation process of the ZCCM proceeded and an ineffective enforcement of existing legal measures for the privatisation of SOEs, had a highly negative impact on the Zambian economy. A more gradual privatisation process would have allowed for the establishment of clear long-term legal rules that would have facilitated the building of effective institutions, required for more successful privatisation and beneficial outcomes (Stiglitz, 1998:19, 22, 2002:182, 183-184; Rose-Ackerman, 1999:44).

5.3 THE ROLE OF THE PRIVATISATION OF THE ZCCM IN IMPROVING PUBLIC FINANCES

The pro-privatisation argument that the privatisation of state assets would have a positive impact in improving public finance would be assessed in the mining sector in Zambia by investigating whether the sale of the mines improved government revenue and reduced the debt of the Zambian government.

5.3.1 Revenue from the sales of the mines

The poor bargaining leverage of the government, mainly because of the weak performance of the ZCCM and of the Zambian economy at the time the mines were privatised, largely accounts for the poor sale price the government was able to obtain for the mines. Of the gross total value of privatisation transactions in 2002 of US$425 million, gross mining sector proceeds accounted for US$338.8 million (79.71%), according to ZPA estimates. However, while the net balance in the Revenue Account/Fund from the privatisation of non-mining assets reached only about US$570 000 on 11 November 2002, with most of the funds in the Revenue Account being used to cover the ZPA and other expenses, no net proceeds remained from the sales of the mines to be transferred to the PRA.

Available information on received proceeds and on the use of funds shows that the gross receipts from the privatisation of the ZCCM, together with other available funds, were insufficient to cover the liabilities of the ZCCM (World Bank, 2002b:22).[337] Because the privatisation of the ZCCM involved asset sales rather than share equity sales,[338] the proceeds from the sale of the mines belonged to the ZCCM, and most of these proceeds were used to cover the company's obligations to various creditors (World Bank, 2002b:22). Accordingly, none of the proceeds from the sales of the assets of the ZCCM benefited the national budget.[339]

The sales agreement that permitted purchasers to pay only a small part of the total cash consideration, with the rest constituting deferred/conditional future payments, also significantly lowered the revenue received from the sales of the mines (refer to Table A5 in Annexure) (Transparency International, 2002:2; ZPA, 2003:2). This practice contravened the Privatisation Act, which stipulates that deferred conditional payment be made available only for Management Buy Outs (MBOs) and the purchase of shares by Zambian nationals. For example, at close, the government received only US$3 million in cash of the total US$28 million agreed upon for the Kansanshi Mine, while US$10 million was payable after completing a pre-feasibility stage and the remaining US$15 million after a feasibility study. Similarly, in the case of the Konkola Division, US$30 million was received in cash at the close of the Anglo American deal, while US$60 million was to be paid in six equal instalments, starting from year six after the closure of the deal (Transparency International, 2002:2).

Moreover, the possibility of deferring payments would disadvantage Zambia if the company exits before paying its deferred cash obligations. This was the case with Anglo American, which left in 2002 after only 18 months of operations at KCM, enabling the Zambian government to obtain only US$30 million from the sale of KCM to the Anglo

[337] Which should be reflected in the cash flows and accounts of ZCCM.
[338] In which case proceeds from the privatisation would have belonged to shareholders.
[339] The government may wish to confirm this through an audit (World Bank, 2002b:22).

American consortium (ZPA, 2003:2). Section 6.3.1 of Chapter 6 shows that the extensive concessions granted to mining TNCs further reduced tax revenue from mining under private TNCs' ownership of the mines.

However, capital investments from mining companies were expected to have more lasting benefits over immediate cash from the sales of the mines, according to the ZPA (2002:6). This argument though is flawed as the failure of foreign mining companies to respect their pledged investment obligations, discussed in Section 6.1 of Chapter 6, severely limited this benefit. Unless the investment is made compulsory, to be agreed before the sales of the SOEs, cash payments take precedence over pledged investments, according to Pennings (2008:484, 489). However, if the proceeds in cash payments are not carefully monitored, as was the case with the ZCCM, corrupt practices may also reduce the benefits of cash payments.

The World Bank blames the poor financial returns that the government gained from the sales of the mining assets on the weak financial state of the ZCCM and its arrears to creditors and utilities. These problems lowered the bargaining leverage of the government to demand more for the mines (World Bank, 2002b:23). However, this argument fails to take into account that the degradation of the assets of the ZCCM occurred to a large extent because of policies of the World Bank and the IMF, which barred the government from investing in mines earmarked for privatisation and not necessarily because of state ownership per se.

It is also likely that corrupt practices, allegedly by top government officials under Chiluba's government, during the privatisation of the ZCCM significantly lowered revenue from the privatisation of the mining sector. It is alleged that public money and proceeds from the privatisation of the mines were siphoned off into private offshore accounts (Afronet *et al*., 2001:14). The above discussion shows that deficiencies in Zambia's regulatory and institutional framework facilitated possible corruption by government officials during the privatisation process.

The fact that the Zambian economy did not gain any net revenue from the sales of the mines contradicts the neo-classical argument that the privatisation of SOEs would increase government revenue from the sales of the assets (World Bank, 2002b:22). It is more in line with findings of empirical studies in sub-Saharan countries that government budgets received only a fraction of the share of privatisation and have at times been wiped out (Buchs, 2003:11). While it is difficult to ascertain what the net income flow would have been under state ownership of the mines, the success of privatisation is certainly limited when a lower sale price is obtained compared to the net income flow that would have been created if the enterprise remained in the public sector (Cook & Kirkpatrick, 2000a:221).

Furthermore, the large-scale corruption that allegedly took place during the privatisation of the mines, within a liberal economy, supports Stiglitz's view that when privatisation occurs with capital market liberalisation,[340] rather than enhancing efficiency, growth and re-investment in the country, the incentive for corporate theft and asset-stripping by insiders increases. Moreover, growth may in fact be depressed (Stiglitz, 2002:144, 155, 158). The determination of a direct causal relationship between capital market liberalisation and corruption is, however, outside the scope of this study. The allegations that money from the proceeds from the sales of the mines was transferred 'offshore' is further in line with Stiglitz's argument that resources might leave the country, as winners of the privatisation process are likely to transfer money to safe havens. This is especially the case when deep depressions contribute to low returns, or when large-scale corruption was involved in the privatisation process (Stiglitz, 2002:144, 157, 158).

5.3.2 The role of the privatisation of the mines in improving public finances

In the short term, the neo-classical argument that the sales of SOEs would improve public finances was not borne out in practice in the Zambian mining sector. On the contrary, rather than reducing its liabilities, the government's assumption of the ZCCM debt of approximately US$770 million, at the completion of the privatisation of its core

[340] Especially when an effective legal infrastructure to ensure good governance is absent.

assets, as part of the consideration of Zambia's HIPC condition, increased Zambia's external debt.[341] The increase was contrary to one of the intentions of the privatisation programme to transfer most of the external loan portfolio of the ZCCM that stood at US$436 million in May 1998, to the new owners (Maambo, 1998:Fig. 7; Transparency International, 2002:6). The government's assumption of the debt of the ZCCM imposed an enormous cost burden on the national budget (Transparency International, 2002:6).[342] Moreover, payment of many of the retrenchment packages and pensions of mineworkers by the government added to Zambia's debt (UNDP, 2001:23; Fraser & Lungu, 2007:10).

More recently, Zambia's external debt was in fact reduced, but not through privatisation and private ownership of the mines. Instead, the Zambian debt was reduced, principally, from the HIPC status[343] for which it qualified in 2005. Additionally, more importantly, because of the MDRI that multilateral institutions extended to Zambia in 2006, a major part of Zambia's debt was written off,[344] after it achieved certain macro-economic, social and governance targets (Transparency International, 2002:6).[345]

The above discussion shows that gains in revenue from the sales of the mines were obliterated and the privatisation of the mines did not improve the debt of Zambia. The main reasons for these were: (i) the poor state of the ZCCM; (ii) the concomitantly lower selling price; (iii) certain concessions granted to mining companies to defer their cash considerations, in spite of these being in contravention of the Privatisation Act; (iv) possible corruption by government officials; and (v) the government's assumption of various liabilities of the ZCCM. Tax concessions also notably reduced government revenue under private ownership of the mines (discussed in Section 6.3.1 of Chapter 6). In the short term, a failure of mining TNCs to respect pledged investments also reduced advantages for Zambia under private ownership of the mines.

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[341] Interviews with Valentine Chitalu, 22 October 2003, Danny Kalyalya, 31 October 2003 and Wilphred Katoto, 12 November 2003.

[342] Interview with Ohene Nyanin, 29 November 2003.

[343] Interviews with Valentine Chitalu, 22 October 2003; Danny Kalyalya, 31 October 2003 and Ladslous Mwansa, 7 October 2003.

[344] Interviews with David Chilipamushi, 20 October 2003 and Valentine Chitalu, 22 October 2003.

[345] Such as using the savings from debt cancellation for anti-poverty programmes through Poverty Reduction Strategy Projects (interview with David Chilipamushi, 20 October 2003).

These outcomes support the arguments of several theorists that increases in government revenue from privatisation would significantly depend on the sale price, adequate taxes, concessions and on the auction designs (Penning, 2008:489; Buchs, 2003:12, 13; World Bank, cited in Cook & Kirkpatrick, 2006:20, 21). However, rather than being due to privatisation as such, the poor gains in government revenue from the sales of the mines seem to be largely attributable to inadequate consideration given to the manner in which the privatisation proceeded and as a result of ineffective institutions. These omissions also facilitated corruption.

5.4 CHANGING OWNERSHIP AND MANAGEMENT STRUCTURE AND THE IMPACT ON MINING PERFORMANCE AND ON THE SOCIO-ECONOMIC DEVELOPMENT OF ZAMBIA

The discussion in this section addresses the research question whether different objectives, organisational capacities and control and monitoring of managers of SOEs over private companies account for better performance of private companies, as is argued by neo-classical theorists. This is followed by an examination of the socio-economic effects of various cost-cutting and profit-maximising measures.

5.4.1 Objectives, organisational capacities, monitoring and control of managers

The roles of different objectives, organisational capacities of mining companies and monitoring and control of managers under changing ownership in influencing company performance are now considered. The examination of these issues under government ownership of the mines is confined mainly to the Kaunda government, as the uncertainty linked to the long transition from the decision to privatise the mines (which commenced shortly into Chiluba's government) to its implementation, weakened incentives and the monitoring of manager behaviour.

5.4.1.1 Impact of different objectives on performance

The investigation of the influences of different objectives under changing ownership on company performance tests the argument of public interest theorists that dissimilar objectives of managers under private and state ownership impact differently on the performance of the company. However, a determination of performance is not easy because of the problem of the counterfactual pre- and post-privatisation, the challenge in selecting appropriate variables to assess performance and the difficulty in isolating the influence of ownership on performance. Moreover, a profit-based determination of performance is complex, mainly because of difficulties in obtaining the relevant statistics largely because of the reticence of private companies to provide information on their profits. Accordingly, instead of an exact quantitative cost-benefit profit-based calculation of performance, the overall performance of mining companies in the study is considered more broadly, by way of the productivity of mineworkers, a lowering in the cost of production or *x*-efficiency and the production levels of copper.

Productivity of workers

Under majority government ownership of the mines during Kaunda's government, higher employment levels that the electoral-maximising motives of the government encouraged, in the absence of improved copper production, reduced labour productivity. Rather than focussing on increasing productivity the Kaunda government greatly prioritised the demands of the mineworkers as a dominant political interest group.[346] Figure 4.21 of Chapter 4 shows that in the early 1980s the excessive employment of workers in the mining sector lowered labour productivity from 9 tons/worker in 1980 and 7.6 tons/worker in 1981 that dropped further in 1991 to 5.9 tons/worker. The decline in labour productivity contributed considerably towards the higher cost of production of the ZCCM over those of its international competitors. Higher employment levels were therefore not sustainable, especially at times of low copper prices and when the mines performed poorly.

However, in the 1990s during Chiluba's government the more effective usage of the reduced labour force (by 11 000 workers from 1992 to 1994), mainly due to rationalisation policies introduced from 1992, in accordance with the SAPs augmented

[346] For instance, despite continued production at some of the mines being achieved at losses, largely to appease the Mineworkers' Union of Zambia, the Kaunda government opted not to close unprofitable mines between 1976 and 1983 to reduce costs (interview with Silane Mwenechanya, 24 October 2003). It also reversed wage restraints of mineworkers in 1975 and it adopted less stringent IMF conditionalities. Furthermore, the 10% wage ceiling measure became possible only with the inclusion of four trade unions to the ZIMCO board in 1983 (World Bank, 1989:27, 33, 43).

the productivity of workers in the mining sector to 7.5 tons/worker in 1993. The uncertainty created from the impending privatisation of the mines though contributed to the poor productivity levels in 1995.

It is further noted from Figure 4.7 and from the discussion in Section 4.4.19 of Chapter 4 that under private ownership of the mines, profit-maximising motives of the shareholders and cost-reduction measures encouraged private managers to reduce even further the number of mineworkers employed. Alongside rising production levels, the additional lowering of the labour force contributed to a notable increase in labour productivity under private ownership of the mines. Labour productivity reached 8.9 tons/worker in 2004.

X-efficiency or reductions in the costs of production of the mining sector

Stronger profit-maximisation motives of private companies and a greater focus on the core business encouraged the private mining companies to pursue greater *x*-efficiency in the mining sector than was the case under government ownership of the mines. Conversely, under government majority ownership, surpluses from mining were diverted away from the core mining sector activities for the development of other sectors to pursue electoral-maximising[347] or political interests and multiple objectives. It is noted in Section 4.3.2 of Chapter 4 that the surpluses were redistributed mainly to develop the manufacturing sector, for social development and for debt service payments of the country.[348] The policies of the Kaunda government to redistribute surpluses from mining for enhancing national, infrastructural and the socio-economic development of Zambians greatly improved the social welfare[349] and the human capital development of Zambians.[350] These policies also promoted the development of the parastatal sector.[351]

However, the deployment of limited mining revenue[352] for developing non-mining sectors, for paying the country's foreign debt and for political purposes, without a

347 Interview with John Lungu, 12 November 2003.
348 Interview with Francis Kaunda, 20 October 2003.
349 Interviews with Danny Kalyalya, 31 October 2003 and Dave Phiri, 23 October 2003.
350 Interviews with Fred M'muembe, 14 October 2003; Dave Phiri, 23 October 2003 and Dennis Wood, 21 October 2003.
351 Especially the manufacturing sector.
352 Interview with Danny Kalyalya, 31 October 2003.

corresponding adequate reinvestment into the mines until they were privatised, was not sustainable. On the contrary, these policies considerably increased the production costs of copper mining in Zambia above those of its global competitors. The redistributive practices, while neglecting to sufficiently reinvest in the mines, also proved detrimental to the productive capacity of the core mining sector that had a negative impact on the performance of the copper mining companies under government ownership, especially at times of low copper prices (Kaunda, 2002:180; World Bank, 2003b:135; Ministry of Finance and National Planning, 2002b:74).[353]

A directing of profits to adequately recapitalise and modernise the machinery and technology of ZCCM,[354] to extend the life of the mines, to develop deep-level mining and to explore for low-cost deposits would have enhanced the longer-term efficiency and sustainability of mining in Zambia. Such measures would also have counteracted the declining ore grades. The Zambian government further failed since the 1980s to invest in research and development activities in the mining sector to promote more efficient ways of mining copper, to lower their production costs and to increase production levels (The Economist Intelligence Unit, 2002:39; World Bank, 2003b:135, 2004a:18; Leistner, 1996:11.12; Kapika *et al*., 1996:7; Maambo, 1998:Fig. 9).

In contrast, high investments that CODELCO undertook in the mining sector in Chile in the 1970s and its research and development activities largely accounted for that country being able to subsequently overtake Zambia in both efficiency and in the production of copper.[355] The costs of production of copper in Zambia rank amongst the highest in the world since the mid-1990s (World Bank, 2003b:135, 2004a:18). The negative impact that the redistribution of limited mining revenue into especially the non-productive sectors had in increasing the cost of production and in undermining the core mining sectors supports the neo-classical argument that electoral-maximising objectives curtail improvements in the performance of SOEs. However, as noted above, the failure to

353 Interviews Andrew Sardanis, 19 October 2003; Valentine Chitalu, 22 October 2003; Alick Lungu, 14 October 2003; Silane Mwenechanya, 24 October 2003; Zion Simwanza, December 2003; Simon Capper, 30 October 2003, Sipho Phiri, 30 October 2003; Silane Mwenechanya, 24 October 2003 and Ladslous Mwansa, 30 October 2003.

354 That had become unreliable and inefficient (interview with Silane Mwenechanya, 24 October 2003).

355 Interviews with Dave Phiri, 23 October 2003 and Kasote Singogo, 16 October 2003.

invest in the ZCCM during the 1990s, while significantly owing to multiple objectives of the government, was also greatly influenced by demands from multilateral institutions that barred investment into the mines that were earmarked for privatisation during Chiluba's government.

On the contrary, greater profit-maximising motives of private mining companies under their ownership of the mines improved *x*-efficiency or reductions in the unit costs of production for a given output of copper at most of the mines in Zambia, compared to the pre-privatisation period (World Bank, 2002a:8; The Economist Intelligence Unit, 2002:39). In particular, a smaller mining operator, Bwana Mkubwa,[356] enjoyed a production cost of US$0.35/lb for copper and of only US$0.18/lb for acid production (after acid credits)[357] in 2001, which made it the most efficient and lowest-cost producer in Zambia. Its low cost of production enabled the company to enjoy operating profits of US$2.64 million at the end of the 2001 financial year, despite the price of copper having reached a virtual all-time low in November 2001 of US$0.59/lb (World Bank, 2003b:132; Africa Mining Intelligence, 2002c:1). The average cost of production of KCM under the ownership of Anglo American, from end-March 2000 until December 2001, also declined by 20% to 30% per pound of copper (from 100 cents to between 70 and 80 cents per pound of copper).[358]

However, despite the improvements in *x*-efficiency achieved under private ownership of the mines, the average cost of copper production of Zambia's mining sector, at 100 cents per pound of copper in 2000, compared to the world price of 84 cents per pound of copper, then still ranked among the highest in the world. The continuing high production costs render Zambia's mines globally uncompetitive (The Economist, 2002b:1). Moreover, in the short term, before 2004, the cost-reduction measures of the private mining companies were insufficient to push most of these companies into profitable positions.

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[356] Which focuses on the processing of tailings through a leaching process.
[357] Bwana Mkubwa sold the excess quantities of acid to other copper producers in the market (World Bank, 2003b:132).
[358] Interview with Lori Hanschar, 18 December 2001.

Irrespective of ownership, a multiplicity of factors such as external factors (mainly the price of copper and cobalt), indirect costs and geo-political factors also played a significant role in influencing the *x*-efficiency and performance of the mining companies. The impact of these factors on performance prevents a more precise determination of the influence of changes in ownership on *x*-efficiency. Indirect costs that lower the global cost competitiveness of Zambia's copper mining sector include higher extraction costs associated with deeper level mining, compared to the open-cast mining[359] that predominates global copper production[360] and the decline in the average copper ore grades linked to deep-level mines. The greenfield mines in the northwest of Zambia (in particular, the Lumwana Copper Mines) that will be developed as open-pit mines promise to be cheaper to operate. They are likely to be on par with the Chilean mines,[361] which cost 40% less than most of the mines in Zambia, partly owing to the predominance of open-cast mining in that country (Africa Analysis, 2002b:16; Africa Confidential, 2002:2; Cherv, 1989:127; World Bank, 2003b:135).

The prohibitive costs of transportation to and from the market and the supply links of Zambia[362] due to the country being landlocked, and the high electricity and fuel costs are further indirect costs that have considerably increased the costs of production of the Zambian mining sector (Africa Analysis, 2002b:16). The impact of the high transport costs on the performance of the mining sector is exacerbated by the fact that most of the plant and machinery inputs required by the mines have to be imported. The high transport costs have also increased the costs of inputs of the highly import-dependent backward-linked industries to the mining sector.

Geo-political factors mainly encompassed the effects of political instability in the sub-region, especially in the 1970s and the 1980s. The subsequent higher transportation

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359 Describes a form of mining in which the mineral is dug from the surface instead of from deep under the ground. It contrasts with deeper level mining (referring to mining at depths in excess of 900 meters) requiring tunnelling into the earth (Science-dictionary.com, 2010; Answer.com, 2010a, 2010b). Asides from rare cases, relative costs (with the exception of quarrying) are significantly less for surface mining, while underground costs are higher. Typically, underground mining costs exceed surface mining costs by a margin of three to four to one (Hartman, 1992:36).

360 Interviews with Valentine Chitalu, 22 October 2003; Silane Mwenechanya, 24 October 2003 and Francis Kaunda, 20 October 2003.

361 Interview with Valentine Chitalu, 22 October 2003.

362 Interview with Francis Kaunda, 20 October 2003.

costs also raised the cost of operations of the Zambian mines and of their backward-linked industries, under government ownership. The closure of Zambia's route links to the south[363] that were used to transport its copper greatly raised the shipping costs of imported inputs[364] under government ownership of the mines (The Economist Intelligence Unit, 2002:4; Seidman, 1977:234, 235). The diversion of shipments from the former Rhodesia, following the Unilateral Declaration of Independence (UDI), cost the government over US$150 million (Seidman, 1977:234).

Costs were further increased due to the poorly functioning road link to the port of Dar-es-Salaam that Zambia was forced to use as an entry port to the sea and because of the difficulties that this port and the railway experienced in trying to cope with the increasing volume of goods.[365] Subsequently, the longer distance[366] through the Tanzania Zambia Railway (TAZARA)[367] opened in 1976,[368] to transport copper and oil as a separate route for Zambia to Dar-es-Salaam[369] further raised the cost of production (The Economist Intelligence Unit, 2002:4; Maambo, 1998:4; McGrath & Whiteside, 1989:169; Van Buren, 2003:1154). Moreover, the sourcing away from South Africa after 1986 in the bid to isolate South Africa's apartheid regime, added another US$60-65 million per annum to the operating costs of the mining sector (Maambo, 1998:Fig. 8; The Economist Intelligence Unit, 2002:5).

Under private ownership of the mines, the factors that obstructed greater *x*-efficiency from being achieved at some mining companies, in addition to the price of copper and indirect costs, included the high toll charges for the processing of ores, owing to Mopani's near-monopoly control over smelting and concentrating activities. Added to

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363 In particular, the limited access to the Rhodesian rail network and other transport links to the south (reopened only in October 1978), in response to sanctions against the former Rhodesia, after the UDI, on 11 November 1965, as well as the closure of the Benguela railway line in 1975 (after Portugal withdrew from its former colony), following the civil conflict in Angola that rendered Zambia's link to the Atlantic port of Lobito in Angola inaccessible (Van Buren, 2003:1154; The Economist Intelligence Unit, 2002:4, 5; Maambo, 1998:4).

364 As mining companies began to airlift heavy machinery and equipment from South Africa.

365 Insufficient traction power, an unsatisfactory safety record, landslides, derailments, severe delays, pilferage and poor management hindered the achievement of greater efficiency of the TAZARA railway (McGrath & Whiteside, 1989:180, 181; Van Buren, 2003:1154). TAZARA incurred losses for the Zambian government in its first eight years of operation but reached a profitable position in June 1983, although it did not consistently achieve profits until 1988 (Van Buren, 2003:1154).

366 Compared to the southern routes.

367 A 1 860 km single-line track, subsequently built by the Chinese.

368 That handled 85% of Zambian exports by 1987, of which 90% was copper. Imports, though, continued to come mainly through South Africa (McGrath & Whiteside, 1989:181).

369 Nevertheless, an improvement to the existing infrastructure.

this were the high costs of obtaining finance that compounded the liquidity problems of mining TNCs. The high costs of corporate skills and unforeseen accidents also increased the costs of some of the private mining companies. Factors internal to the operations of private mining companies, such as operational problems and poor decision-making, further limited the achievement of greater *x*-efficiency at some private mining companies. Notwithstanding that the high cost of rehabilitating the mines increased the production cost of the mining sector under private ownership, the extent of its influence in the short term is questionable. This is because in the short term, capital investment under private ownership was not much higher than in 1991 under government ownership during Kaunda's government (refer to Figure 4.11 of Chapter 4 and the discussion bin Section 6.1.2 of Chapter 6).

Accordingly, declining profit in the mining sector in Zambia cannot be definitively attributed to state ownership as other factors also influenced the mining sector adversely. This conclusion is supported by the application of the ROCIPI research programme to the Zambian parastatals, which shows that the failure of parastatals in Zambia reflected not the simple character of ownership but rather the complex interaction between national policy, economic realities and management intent, according to Makgetla (1994:123). The strong impact of factors additional to ownership on the poor economic performance of the ZCCM, from the 1980s onward and especially in the 1990s, also vindicates the argument of Cook and Kirkpatrick (2004:211) that a complex of other factors besides ownership also influenced efficiency.

<u>The influence of different ownership on copper production</u>

The production levels of copper and factors influencing these are examined below to test the argument that privatisation would result in lower output levels, since the government no longer subsidises firms to maintain output levels also at inefficiently high levels, according to Boycho *et al*. (1993, cited in Boubakri *et al*., 1999:20). The testing of public interest theory that output increases under government ownership, due to economic welfare-maximising objectives of the government (by maximising the output level of the firm at a socially optimal level, within a given cost structure) that has relevance in the utility sectors has limitations in the resource sector. This is because the price of copper is determined on the international market and the consumers of copper are almost exclusively foreign. Moreover, the impact of other factors apart from ownership on copper production obscures discernible trends in the relationship between ownership and production levels of copper. The discussion on the influence of different ownership on copper production is therefore tentative, meriting more in-depth research outside the scope of the study.

Notwithstanding the impact of various additional factors on the output levels of copper, ownership still seems to play some role, although a rather complex one, in influencing production levels. Figure 4.18 shows that during Kaunda's rule, the production levels of copper increased considerably in the 1960s, reaching a peak of 747 500 tons in 1969 when the government took over majority ownership of the mines, from 680 000 tons in 1965. The production levels continued to be high in the 1970s as well. High copper prices were mostly responsible for the large increases in production levels in the 1960s. Under state ownership of the mines, electoral-maximising motives such as the decision to continue production at some loss-making mines, largely to appease the mineworkers, also promoted higher production levels. Figure 4.19 shows that the Kaunda government likely cushioned production levels in 1982 and in 1989.

However, these high production levels were not sustainable under government ownership of the mines. A significant decline took place in copper production levels especially from the 1980s,[370] following the adoption of IMF/World Bank policies from 1983-87 and again from 1989-91, with an increasing decline taking place in the 1990s under Chiluba's government (World Bank, 2002b:9, 2003b:134). The contraction of copper production in Zambia was particularly severe in the latter part of the 1990s and in 2000 under private ownership of the mines. Subsequently, production levels increased again under private ownership of the mines.

Certain omissions under government ownership of the mines that diminished the role of

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[370] Despite the growth of copper production at a rate of 7.6% p.a. from 1985-90.

mining as a long-term source of revenue undermined the sustainability of high production levels. These included insufficient regard for improving the performance of the mining sector and for saving a portion of their returns. The savings of some of the returns would have lowered to some extent the negative consequences of low copper prices on the performance of the mining sector. Furthermore, in particular during Chiluba's government in the 1990s, the lack of resources that limited reinvestment in the mining sector and the increasing costs of production obstructed higher production levels. The lack of adequate resources for reinvestment also largely accounted for the weaker response in output to higher copper prices during Chiluba's government, compared to under Kaunda's government and under private ownership of the mines during the boom (Figure 4.19 and 4.20), elaborated upon in Section 4.4.18 of Chapter 4.

While the government would for political reasons be less inclined under government ownership to significantly reduce production levels, to protect the workforce, under private ownership of the mines, certain *x*-efficiency and profit-maximising objectives of companies might, at times, constrain higher production. The private sector's preference for profit-maximisation over higher employment levels would also likely result into production levels becoming more responsive to declines in copper prices under private ownership of the mines. For instance, in the short run, the temporary closures of the mines[371] that were more dominant under private ownership and the withdrawal of some mining TNCs[372] from Zambia to cut costs or promote profit-maximising motives considerably influenced reductions in the production levels of copper in 2000.

The production of copper reached its lowest levels since the 1950s under private ownership of the mines at the end of 2000, at 257 000 tons (The Economist Intelligence Unit, 2002:40; Ministry of Finance and Economic Development, 2000:60; Pretoria News, 2004:21). The low copper prices in the late 1990s and in the 2000s though also influenced the poor production levels at the time. However, after the dip in the copper price in 2000, copper output increased from 298 000 tons in 2001 to 409 500 tons in 2004 and to 497 169 tons in 2006.

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371 Such as the temporary halting of production at the Chibuluma mines, in September 2001 and the closure of the Nkana smelter.
372 As was the case with Anglo American.

The record high international copper prices from 2004 to 2006, together with higher investments or rehabilitation of the mines, undertaken in 2004 significantly influenced the notable increases in copper output in Zambia during these years (The Economist Intelligence Unit, 2007b:4, 30; 2008b:19, 25, 30, 34; Fraser & Lungu, 2007:1, 19). Also, although the production figures in 2004 and 2005 were higher than those achieved just prior to the privatisation of the ZCCM these levels were not unusually high in the history of copper mining in Zambia (Fraser & Lungu, 2007:19). Copper production levels at 445 600 tons in 2005 were only slightly above the 421 500 tons attained in 1990, and were lower than the 1989 level of 448 400 tons.

Nonetheless, the greater resources of private mining TNCs, in particular their much needed capital and technology contributions into the mines[373] (elaborated upon in Section 6.1.2 of Chapter 6 and Table A9 in Annexure) might increase production levels. The higher capital and technology stock would also promote greater sustainability of the mining sector (The Economist Intelligence Unit, 2008a:7). On the flipside, Section 6.1.2 of Chapter 6 assesses briefly the likelihood that improved company performance under private ownership may also raise the necessary revenue to enable greater technological investment in the mines.

As is observed above, production levels of copper were also significantly influenced by factors other than ownership, in particular the price of copper and cobalt. Moreover, the high costs of Zambia's copper industry, beyond those of most global competitors, together with decades of underinvestment and an ageing infrastructure, render the prospects of Zambia's copper industry highly dependent upon the future price of copper (The Economist Intelligence Unit, 2007b:30, 34). The near closure of depleted mines such as the Nchanga open pit at the end of its life cycle and the increasing substitution of copper by fibre optics that is taking place in recent years would also lower production levels of copper, independent of ownership.

[373] That would enable mining TNCs in the longer term to open new mines, to recapitalise and to expand existing mining entities that would make deeper mining possible, and improve company performance.

Further factors irrespective of ownership that affected copper production levels, extracted from Section 4.4.17 of Chapter 4, were:

- The opening of new sources
- Increased costs caused by poorer quality ores and more expensive methods of mining associated with deeper-level mining from the mid-1980s
- The lack of capital for reinvesting in the mines (also the case with some mining TNCs), which was especially severe in the 1980s and the 1990s
- Delays and difficulties experienced in obtaining imported spare parts or inputs[374]
- Flooding problems in the mines[375]
- Power shortages
- The inaccessibility and inefficiency of the infrastructure supporting the mining sector
- Accidents
- A high silica content in the ores, in late-1996
- Labour unrest (The Economist Intelligence Unit, 2008a:6, 7, 2008b:19).

The influences of various factors also other than ownership on output, the positive impact of the unprecedented boom in the copper price[376] and the short span within which the private companies operate the mines precluded definitive conclusions as to the impact of private ownership on production levels[377] within the confines of the study. The determination of output performance based on the short-term performance improvements may therefore suffer from a demonstration effect, providing a misleading indication of performance under private ownership of the mines. It is though noted above that at times of weak copper prices and poor performance the possible closures of mines, more likely under private ownership than under state ownership, owing to the electoral maximising motives of the state that do not favour closures, would likely suppress rather than promote production levels.

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374 Especially the shortages of heavy fuel oil (HFO) and of low matte grade concentrates and of acid, under both private and government ownership of the mines, mainly in the 1990s, which resulted in unscheduled shutdowns, particularly at the Mufulira smelters in 1999.

375 The Zambian mines are some of the wettest in the world.

376 Eliciting a high supply elasticity in the volume of copper output.

377 And on the supply elasticity of copper (or the responsiveness of the volume of output to price).

In summary, the above discussion shows that private mining companies were more successful in achieving greater productivity of workers and *x*-efficiency than was the case under government ownership of the mines. While the redistribution of mining surpluses to develop other sectors, for electoral-maximising motives, under government ownership promoted greater development of the Zambian economy, these activities were unsustainable at times of low copper prices and had a negative impact on growth in the mining sector. Moreover, these objectives of the government curtailed greater reductions in the costs of production or *x*-efficiency. However, the influences also of factors independent of ownership on mining performance, confounded a clear determination of the extent of the influence of multiple and electoral-maximising objectives of the government in reducing mining performance. Not only the reductions in labour costs that the private companies mostly tended to target but all the factors that impinged on the performance of the mining sector required to be addressed for achieving greater *x*-efficiency and better performance in the mining sector.

Furthermore, it can be concluded from the above discussion that in instances of high copper prices, the electoral-maximising motives of the state to maintain high employment levels of mineworkers favoured higher production levels during Kaunda's government. At times the government cushioned higher production levels even when the price of copper dropped. However, the government was unable to sustain such high production levels in the longer run, especially when the copper prices fell and when it lacked adequate capital.

Inadequate measures to increase the growth of mining companies through higher productivity, greater *x*-efficiency and reinvestment into the mining sector and to encourage the savings of a portion of mining surpluses, undermined the sustainability of higher production levels under government ownership. Growth and savings are therefore crucial for enabling the government to better manage the influences of other negative factors on the mining sector and for promoting greater sustainability of high production levels of mining, in the long term. Meaningful conclusions also cannot be drawn as to the relation between private ownership and production levels mainly because of the highly significant influence of the copper price boom in improving production levels and due to the short time that mining TNCs operate in Zambia.

5.4.1.2 Organisational weaknesses

The argument that greater organisational weaknesses also promote poor performance of SOEs is considered in the context of the more bureaucratic decision-making under government ownership, the political influence of the government in the operations of the mining companies and of the Zambianisation policies that the government adopted under government ownership of the mines.

- *Bureaucratic decision-making*

A bureaucratic decision-making approach and the lack of autonomy necessitating referral to a committee for each decision made at the ZCCM,[378] lowered productivity and efficiency under government ownership of the mines.[379] Poor collaboration and diverse and the often competing views of the Finance Ministry[380] and the National Commission for Development Planning (NCDP)[381] further stifled quick decision-making. Government interference, especially in aspects of marketing, sales, production, and finances and in the production targets of the ZCCM, decided at the corporate Head Office, also limited management autonomy.[382] In contrast, the greater autonomy of managers under private ownership led to swifter, more efficient decision-making. The bureaucratic decision-making under state ownership of the mines supports the pro-privatisation theorists' argument that SOEs lack management autonomy, contributing to greater organisational weaknesses in SOEs.

- *Political influence in the operations of mining companies*

Political influences motivated by electoral-maximising objectives that took precedence over profit-maximising motives in the operations of the mining sector under

378 Interview with Wilphred Katoto, 12 November 2003.
379 Interview with Chama Kapambwe, 11 November 2003.
380 Responsible for the current budget and the government's cash positions.
381 Whose mandate was to manage the capital budget and the body was concerned with promoting planned targets, financed largely by overseas and external borrowing.
382 Interview with Silane Mwenechanya, 24 October 2003.

government ownership and management have also hindered profit-based performance. Political influence however was deemed necessary on account of the strategic importance of the mining sector. The government was able to promote political interests in the mining sector through the dual position of the Chairman and Chief Executive of the copper mines, a political appointee,[383, 384] and his role as Chairman of the company's board. The political agendas under government majority ownership of the mines limited the influence of the private sector. The more than two-thirds government control of the board of the copper mining company[385] further increased the influence of the government over that of the private sector members on the board.

- *The influence of Zambianisation policies*

Furthermore, in the short term weaknesses in the Zambianisation policies (that the government introduced) also lowered productivity. The Zambianisation policies favoured indigenous Zambians over expatriates, while mining TNCs generally tend to employ expatriates over locals in management positions under private ownership (elaborated upon in Section 6.3.3.2 of Chapter 6). Expatriate employment levels in the copper industry declined from 16% in 1964 to 10% in 1971 and to 3.5% in 1983.

In the initial stages, the Zambianisation policies contributed to inefficiencies in the mining sector due to reduced know-how as the inexperienced indigenous Zambian labour force replaced the experienced expatriate staff, which increased production costs.[386] In the absence of an educated and trained Zambian workforce, expatriate skills were crucial. Moreover, skilled jobs became fragmented with less clear-cut responsibilities under government ownership (Economic Development Institute of the World Bank, 1989:19; English, cited in Wohlmuth and Messner, 1996:429). However, the 'fragmentation' was also because of expatriates deliberately creating alternative vacancies for Zambians in order to retain their own positions. The Zambianisation policies also affected a rise in the supervisory positions from 1 598 in 1982 to 2 268 in

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383 Interviews with M. Shandavu, 10 October 2003; Silane Mwenechanya, 24 October 2003; Charles Muchimba, 18 November 2003; Bernadette Mwakacheya, 17 October 2003 and Andrew Sardanis, 19 October 2003.
384 Interview with Silane Mwenechanya, 24 October 2003 and Dave Phiri, 23 October 2003.
385 Interview with Andrew Sardanis, 19 October 2003.
386 Interview with Fred M'muembe, 14 October 2003.

1993, increasing the superior/subordinate ratio from 1:35 in 1982 to an all-time high of 1:16 in 1993 (Kapika *et al*., 1996:3).

However, it is erroneous to blame Zambianisation policies for the inefficiencies that occurred at a later stage. As is noted in Section 4.2.1 of Chapter 4, rather than contributing to a decline in productivity over the medium to long term, the extremely effective training provided to indigenous Zambians to speed up the Zambianisation policies promoted high competency of Zambian managers. These training policies were also responsible for the commendable and successful development of a highly skilled labour force, especially in the mining sector. The training enabled a merit-based selection of Zambian managers[387] at the operational level, taking into account their competence, skills, qualifications, and mining experience.[388] The extension to Zambians of benefits which had been reserved for expatriate personnel before the state's takeover of the mines (refer to Section 4.2.1 of Chapter 4) and the greater economic control that Zambian employees gained in mining as a result of Zambianisation policies, served as an important means to improve performance of Zambian managers under government ownership.[389]

5.4.1.3 <u>The monitoring and control of managers</u>

Property rights theorists, who place greater emphasis on the principal-agent relationship than on ownership, consider better incentives provided to private management as an important incentive for improving company performance. The importance of incentives in improving company performance has led several theorists to conclude that adequate incentives to managers would improve company performance irrespective of ownership. The takeover constraint is considered as a further important mechanism to encourage managers to pursue profit-maximising motives, according to pro-privatisation proponents. The discussion below examines whether better incentives were provided to

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[387] Interviews with Francis Kaunda, 20 October 2003; Silane Mwenechanya, 24 October 2003; John Lungu, 12 November 2003; Andrew Sardanis, 12 November 2003; Charles Muchimba, 18 November 2003; David Chilipamushi, 20 October 2003 and Bernadette Mwakacheya, 17 October 2003.

[388] Those that benefited from scholarship programmes were employed mainly at the operating levels, rather than at the executive decision-making levels (interview with Andrew Sardanis, 19 October 2003).

[389] Interviews with David Chilipamushi, 20 October 2003; Silane Mwenechanya, 24 October 2003; Wilphred Katoto, 12 November 2003 and Dave Phiri, 23 October 2003.

managers under private ownership of the mines, the influences of better incentives through private management of the mines while under government ownership between 1970 and 1973, and the role of the possibility to takeover a company under private ownership in promoting improved company performance.

Under government ownership and management control of the mines, much like under private ownership and management, the board of the company (made up of both the government and the private sector, comprising of the Anglo American directors and/or other minority shareholders),[390] monitored and controlled managers. However, the high priority placed on promoting political interests and electoral-optimising objectives in the government-dominated board redirected the managers' objectives away from greater profit-maximising. Moreover, the government's reluctance to replace managers who did not make a profit further promoted inefficiencies.[391] Poor incentives to managers in the late 1980s, reflected in reductions in real wages of senior officials to 51% of the 1967 levels, also served as a disincentive for attracting more skilled employees (Economic Development Institute of the World Bank, 1989:16, 18, 19).

In contrast, vastly superior incentives were provided to managers under private ownership, which pro-privatisation proponents argue encourage them to pursue the profit-maximising objectives of their principals, namely their shareholders. The incentives provided to private managers include better social benefits and salaries that are predominantly dollar-based,[392] monetary share options[393] and bonus schemes[394] (also based on performance appraisals,[395] whereby managers receive a certain percentage of the profit over a target rate in their area of operation). A contractual managerial employment approach at Mopani (for a two-year duration) and at Bwana Mkubwa (on an open-ended basis), adjusted annually depending on the performance of managers,

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390 Interviews with Wilphred Katoto**,** 12 November 2003; M. Shandavu, 10 October 2003 and Bernadette Mwakacheya, 17 October 2003.

391 Interview with Zion Simwanza, December 2003.

392 At Mopani (interview with Emmanuel Mutati, 18 November 2003).

393 At First Quantum (interview with Andrew Hickman, 7 November 2003).

394 At AVMIN (managers, however, failed to enjoy this benefit since the company was largely making losses).

395 At Copperbelt Energy Corporation (CEC). Performance appraisal incentives in the form of cash bonuses provided to both managers and workers at CEC are established through managers together with all the workers in their division both setting and trying to achieve certain targets set by the companies and themselves, which encouraged teamwork (interview with Gary Loop, 29 October 2003).

represents a further incentive to encourage improved manager performance.[396]

Under private ownership of the mines, the listed companies seemingly boast superior measures for monitoring and controlling manager behaviour over non-listed companies. Alongside normal internal controls through their board of directors, listed companies are also subject to international standards of controls also through their foreign shareholders. In addition to the requirement of sound finances and profitability, the international controls subject these companies to audits and the scrutiny of bankers, who demand good social and environmental policies before extending loans to companies.[397] The company code of conduct, the disciplinary code and various other firm-specific measures, determined through the board of the company, impose further controls on manager behaviour.

On the other hand, between 1970 and 1973 private management by expatriate managers under minority TNCs' shareholding (then 49%) and 51% government ownership of the copper mines in Zambia did not represent an important incentive for improving company performance. On the contrary, certain strategies of the expatriate managers undermined greater improvements in the performance of the local mining companies. The stronger motivation of expatriate managers to improve the income of the shareholders of the mining TNCs over those of the local mining companies reduced gains for Zambia from mining surpluses and dampened better performance of the Zambian mines between 1970 and 1973 (refer to Section 4.2.1 of Chapter 4).

The higher income for parent companies of mining TNCs was orchestrated firstly through strategies of managers to manipulate the profits of the mining companies, predominantly through transfer-pricing policies and by way of inflated service fees (management, consulting and marketing privileges) that the parent companies enjoyed. The exclusive rights granted to the parent companies in the provision of these services enabled the high fees that artificially increased the cost of local production. Secondly, the mining TNCs repatriated a large portion of their share of profits to their parent

[396] Interviews with Emmanuel Mutati, 18 November 2003 and Andrew Hickman, 7 November 2003.
[397] Interview with Andrew Hickman, 7 November 2003.

companies (which supplemented their income) or as dividends to their foreign shareholders instead of using it for reinvestment in the mining sector. The dampening of the growth in performance of the copper mines as a result of these practices contrasts with the successes of corporatisation and commercialisation in improving company performance in New Zealand and Poland.

The lack of appropriate government policies and oversight to provide for the development needs of the country, especially in respect of allowing mining companies to repatriate profits out of Zambia and in curbing transfer-pricing policies, also assisted the externalisation of profits from mining. The preferential treatment granted to mining TNCs to automatically externalise non-taxable profits, dividends, management fees and income from the sales of copper, facilitated the repatriation of profits (Sardanis, 2003:268, 269; Saasa, 1987:40; Turok, 1989:47). Accordingly, private management per se is not a sufficient condition for better company performance and may, in fact, contribute to further declines in performance, through transfer-pricing practices. Better company performance under foreign private management of the mines also required effective government control to curb against both transfer pricing practices and the extent of the externalisation of mining profits out of Zambia.

Moreover, contrary to the argument of neo-classical theorists that the possibility of a takeover acts as an effective constraint against poor performance of private companies, the takeover constraint did not represent an effective deterrent against poor performance in the newly privatised mining sector. For example, despite the superior incentives and controls of managers of private companies, RAMCOZ performed poorly (discussed in Section 6.1.3 of Chapter 6). However, it could be argued that the alleged corrupt relation that RAMCOZ had with the Chiluba government afforded the company leeway for engaging in these activities, without effective retribution.[398]

Furthermore, the poor performance of RAMCOZ under private ownership did not, as is argued by pro-privatisation proponents, result in a smooth takeover but imposed a huge

[398] Interview with Ohene Nyanin, 29 November 2003.

cost on the Zambian economy. This was mainly due to the delays and difficulties that the government experienced in getting new private sector interests to take over Luanshya/Baluba.[399] The finalising of the deal with J and W in the acquisition of both RAMCOZ and Chambishi Metals plc for an undisclosed sum was slow, with J and W taking over control of Chambishi Metals only in 2004, despite having signed a memorandum of understanding on 9 April 2003 (Africa Analysis, 2003c:3; Africa Mining Intelligence, 2003c:2, 2003d:1; Africa Research Bulletin, 2003b:15600). Also, Vedanta took over KCM only two years after the departure of Anglo American from Zambia in 2002. The delay in the private sector takeover of especially RAMCOZ had far-reaching adverse social consequences, discussed in Section 6.1.3 of Chapter 6 (CCDJP, 2002a:4; The Economist Intelligence Unit, 2002:40).

The failure to achieve a smooth and quick takeover indicates a weakness in the neo-classical argument that a takeover constraint acts as an effective deterrent or a discipline against poor management performance under private ownership. Rather, the case of RAMCOZ supports the view of Cook and Kirkpatrick (2000a:210-211) that the takeover constraint does not act as an effective deterrent against poor manager performance. It also vindicates the argument that the takeover constraint is ineffective in developing countries (partly because of uncompetitive capital markets in these countries), according to Vickers and Yarrow (1988:24).

5.4.2 Socio-economic effects of cost-cutting or profit-maximisation objectives of private companies

In the absence of a greater redistribution of benefits from improved performance of mining companies, several cost-cutting (or *x*-efficiency) and profit-maximising measures that the private mining companies adopted, whilst enhancing company performance, had adverse socio-economic development consequences for Zambia. The following discussion examines the socio-economic and development consequences of the dominant cost-reduction and profit-maximisation objectives of private mining companies.

399 Interview with Bernadette Mwakacheya, 17 October 2003.

The main methods by which mining TNCs reduced their production costs were through: (i) concessions; (ii) reductions in the labour force and a lowering of their conditions of employment; (iii) shifting some responsibilities for the payments of retrenchment and pension packages, as well as for the provision of social services and for the treatment of some pollution, onto the government; (iv) temporary closures and withdrawals of mining companies; (v) supporting foreign suppliers over local suppliers; and (vi) a depreciation of the kwacha. Each method is now discussed in greater detail.

- *Concessions*

The concessions granted to private mining TNCs (elaborated upon in Section 6.2.2 of Chapter 6), greatly reduced the production costs of the mining TNCs. However, the concessions had a highly negative impact on government tax revenue and subsequently on the development of Zambia (Section 6.3.1 of Chapter 6). The concessions amounted to a government's subsidisation of the private mining TNCs.

- *Reductions in the labour force and a lowering of conditions of employment*

In addition to the concessions, the layoffs of many mineworkers, including highly skilled employees,[400] to improve worker productivity and reduce the total expenditure of their wage bills[401] represented a further main strategy that private mining companies employed to reduce their production costs (World Bank, 2002b:19; ZPA, 2002:3).[402] However, it is noted from Section 4.4.6 of Chapter 4 that the significant numbers of retrenchments in the mining sector were already instituted under government ownership during Chiluba's rule, in the transition period that led towards the privatisation of the mines. Figure 4.7 of Chapter 4 shows that about 14 400 mining employees lost their jobs at the ZCCM between 1992[403] and 1996 before the mines were even privatised (from 62 100 to 47 700). However, these retrenchments were spurred largely by fiscal pressure that SAPs imposed on the government to cut government expenditure at the

[400] Interview with Norman Mbazima, 18 December 2001.
[401] Interview with Willie Sweta, 30 October 2003.
[402] Interviews with Alick Lungu, 14 October 2003; Dennis Wood, 21 October 2003; Jack Jones, 22 October 2003 and Silane Mwenechanya, 24 October 2003.
[403] Sources other than the CSO, though, show less significant increases in the employment levels in the early 1980s and a lesser decline in mining employment from 1993.

ZCCM[404] and partly in preparation for the privatisation of the mines (Catholic Secretariat, 2001:17; ZPA, 2002:3).

In the light of the poor and highly volatile copper prices in the late 1990s, these adjustments to reduce labour might have been necessary to improve the poor performance of the copper companies. A weighing of the real adjustments required to optimise the performance of the mining companies and of false efficiencies (a topic outside the scope of this study), would provide a more accurate portrayal as to whether these adjustments benefited or imposed a higher cost on the country as a whole. In the case of false efficiencies, the overall and social costs to the economy as a result of the huge job losses would beyond a certain threshold outweigh the benefits of improved company performance to the Zambian economy.

At the commencement of the privatisation of the mines, a further 8 540 mining employees lost their jobs between 1996 and 1998 under a government-World Bank programme that the private companies made conditional on the sale of the mines, and another 639 employees lost their jobs in 1999 (Afronet *et al.*, 2001:18, 34; ZPA, 2000b:16; Fraser & Lungu, 2007:21). Moreover, from 1998 to 2002 a staggering 20 160 mineworkers lost their jobs under private ownership, with permanent employment in the mining sector falling respectively from 39 160 to only 19 000. By September 2006, at the peak of the high copper prices, permanent employment in the mines rose only slightly to 21 000, still lower than the 2000 figure of 22 000 and much lower than the permanent employment level of 38 521 workers in 1999. Accordingly, the expectation that the private mining companies would substantially increase permanent employment opportunities for workers is unlikely to materialise, since much of the retrenchments occurred precisely as a result of mining TNCs downsizing their operations.[405]

Increases in the employment of foreign contractors for much of the work previously

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404 Interview with Francis Kaunda, 20 October 2003.
405 Interview with John Kangwa, 21 November 2003.

done by the mining companies themselves,[406] the shifting of many workers onto rolling, fixed-term contracts[407] and an increasing casualisation of the workforce further lowered the labour costs of private mining companies. In 2006, the total mining sector labour force consisted mainly of external contract workers (41%), fixed-term workers (5%) and casual workers (1%). In 2006, permanent employment made up only 53% of the total mining sector labour force in Zambia (Fraser & Lungu, 2007:22, 24).

The rise in the total employment levels in the mining companies in more recent years was mainly attributable to the phenomenal increases in employment in external contract firms. In 2006, the mining companies indirectly employed about 16 000 workers via contracting firms (that increased from 2 628 in 2000 to 11 536 in 2004) and at least 1 900 workers on either fixed-term contracts, varying in duration from one to 5 years, or as seasonal/casual labour (Fraser & Lungu, 2007:22, 49). While just over half of the workforce of most of the major mining companies consists of permanent workers, Non-Ferrous Company-Africa (NFCA) and Bwana Mkubwa employed more contract workers than permanent workers in 2006.

Of the 1 019 employees directly employed by NFCA in 2006, only 232 workers made up the permanent workforce; 687 employees were employed on a fixed-term basis and a further 100 workers were employed as casual workers. Accordingly, the permanent workforce comprised of only 29.7% of the employees directly employed at NFCA and made up only 10.5% of the total workforce of 2 200 workers directly and indirectly employed at NFCA. The two Chinese subcontracting firms that indirectly performed extensive work for NFCA employed 1 093 workers in 2006 (Fraser & Lungu, 2007:49). Also, in 2003, Bwana Mkubwa employed between 300 and 400 subcontracted workers on site, while the permanent workforce consisted of only about 200 Zambians.[408] The contract firms in the mining sector continue to make extensive use of fixed-term contracts, hiring many ex-miners to do the same jobs at the same site where they had

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[406] Interview with Agnes Bwalya, 9 November 2003.
[407] Interview with David Chilipamushi, 17 December 2001.
[408] During that time, an additional 200 to 250 Zambians were employed on a subcontracting basis to haul ore from the Democratic Republic of Congo (DRC) (interview with Andrew Hickman, 7 November 2003).

previously worked, but on non-permanent contracts (Fraser & Lungu, 2007:22).[409]

Whereas permanent workers are entitled to pensions and union representation and enjoy wages above poverty levels,[410] external contract workers and fixed-term workers continue to experience substantially less beneficial terms and conditions of work. However, the wages of permanent workers have also not increased in line with the improved performance of the mining sector. The wages of permanent workers at NFCA were the lowest of all the mining houses in Zambia.[411] To date, the full-time contract workers are also exposed to less favourable conditions of employment than their counterparts in the mining houses (Fraser & Lungu, 2007:48).[412]

Most significantly, in 2006 the wages of non-permanent workers were in some instances just 10% of those offered to permanent workers, for the same work at the same mine. Moreover, they are still not entitled to pension benefits (Fraser & Lungu, 2007:22, 23, 45, 48, 49; The Economist Intelligence Unit, 2008b:21).[413] The non-permanent workers are further deprived of the benefits such as union representation and access to medical insurance or free treatment for their dependants and other fringe benefits, including patient cover and housing,[414] which most permanent workers enjoy (Fraser & Lungu, 2007:3, 20, 22, 23, 53). Additionally, mining companies neglected to take responsibility for the conditions of work of workers in subcontracting companies (Fraser & Lungu, 2007:25).

Limitations placed on the unionisation of workers[415] and the ability of the mining companies to dismiss non-unionised workers without paying them severance

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[409] For instance, in 2006, the permanent workforce at Mpelembe Drilling comprised of around 600-800 workers, while over 1 000 employees were employed on fixed short-term contracts (MUZ, cited in Fraser & Lungu, 2007:23).

[410] Established by the Basic Needs Basket (BNB). The figure is derived from the cost of basic food items and non-food items, such as charcoal and soap, and the costs of housing, water, electricity, education, health and transport to work, for an average Zambian family of six (Fraser & Lungu, 2007:23).

[411] Earning just above the costs of the Basic Food Basket (BFB), a figure that covers food items alone.

[412] In particular at BGRIMM Explosives, Sino-Metals and a number of other contractors that NFCA employ in the 'Chambishi Investment Zone.

[413] The wages of many casual or contract workers that are directly employed at NFCA comprised of merely 10% of the Basic Need Basket in 2006, significantly below the legal minimum wage (Fraser & Lungu, 2007:49).

[414] However, they are given a housing allowance (Fraser & Lungu, 2007: 22).

[415] Achieved mainly through the massive reduction in the permanent workforce in mining and by degrading the power of unions representing the mineworkers, through the practice of these companies to dismiss the 'shadow committee' of employees (required to be formed for union recognition), which forces the MUZ, once they have identified a shadow committee, to organise clandestinely.

allowances, and difficulties experienced in organising collective action[416] have further lowered the conditions of employment of workers. These limitations also diminished the power of the unions to demand better working conditions for mineworkers (Fraser & Lungu, 2007:24, 25, 26, 52). Also, cost-reduction objectives of private mining companies that encourage the employment of temporary or casual workers in the underground mines, especially at NFCA, have degraded safety considerations (that were pivotal under government ownership).

Poorer safety considerations possibly account, alongside the failure of the formal regulatory bodies to implement safer working conditions, for the increases in accidents[417] at some of the mining companies under private ownership (Fraser & Lungu, 2007:49).[418] Moreover, under private ownership the huge unemployment of mineworkers and a lowering of their conditions of work to reduce costs eroded job security and created, for the first time, a category of 'working poor' amongst mineworkers and compounded increases in poverty levels (Fraser & Lungu, 2007:3, 10).

- *Shifting responsibilities of retrenchment and pension packages onto the government*

The cost-reduction strategy of some private mining companies of shifting the responsibility for the retrenchment and pension packages of the mineworkers onto the government, as a pre-condition before finalising the sales of the mines, was at a huge cost to the national economy (Fraser & Lungu, 2007:21, 22). This was especially the case in the context of the high external debt of the Zambian government. The government paid the retrenchment packages of those workers that were retrenched before the mines were privatised largely through a World Bank loan, taken out

[416] Owing to the non-obligatory nature of the right to recognise trade unions, difficulties experienced in organising workers employed in subcontracting firms and cumbersome requirements before a strike can occur. These requirements include an agreement by both parties on the next course of action; a 10 day waiting period subsequent to the unions securing a 2/3 majority from the workers before workers are allowed to strike; and the possibility that the Minister could stop the strike during this time, through the courts, if deemed against the interests of the public.

[417] In 2005, 78 fatalities occurred as a result of mining accidents that were largely attributable to the explosion at the BGRIMM plant that killed 52 Zambian workers, the single biggest disaster in the history of Zambian mining (Fraser & Lungu, 2007:24, 26, 28).

[418] Interview with Zion Simwanza, December 2003.

specifically for this purpose.[419, 420] All the retrenched workers had received their retrenchment packages by the end of 2003.[421]

However, mainly as a result of the tight budget constraints of the government, thousands of former workers of the ZCCM had not been paid their pensions by 2006 (Fraser & Lungu, 2007:3). Furthermore, the policy of the mining companies of subtracting personal and holder vehicles and loans and the costs of houses previously owned by the ZCCM but sold to their former employees, from their retrenchment packages and the deduction of the houses from their pension packages as well greatly reduced the retrenchment and pension packages of former employees (Fraser & Lungu, 2007:30, 51). In addition, some mining companies, such as Metorex, paid only part of the pensions of their workers, calculated from the time they took over their respective mines, while the government had to pay the rest (Fraser & Lungu, 2007:5, 31). Moreover, delays by mining companies that privatised earlier, such as RAMCOZ and NFCA, in paying the retrenchment and pension packages of laid-off workers,[422] brought about severe financial difficulties for the affected former employees of the ZCCM (Lungu, 2001:6).

Accordingly, the safety nets provided to those left unemployed were absent or highly inadequate in dealing with the difficulties that the mining community faced subsequent to the liberalisation of the economy and the privatisation of the ZCCM. Moreover, transferring the obligation for the payment of some of the retrenchment packages and of the pensions of those mineworkers that were retrenched to the government contributed considerably to the zero net gains of the Zambian government from the proceeds from the privatisation of the mines (UNDP, 2001:33). On the contrary, these practices, together with measures forcing the government to treat the pollution of some mining companies, exacerbated the debt of the Zambian government.

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[419] Interviews with Emmanuel Mutati, 18 November 2003; Fortune Kamusaki, 25 November 2003 and Danny Kalyalya, 31 October 2003.

[420] The World Bank also provided a loan to address environmental issues in the mining sector (interview with Danny Kalyalya, 31 October 2003).

[421] BoZ, questionnaire, 3 December 2003.

[422] AVMIN paid the severance packages of workers immediately after takeover.

- *Reducing responsibilities in the provision of social services*

Under private ownership, profit-maximising motives encouraged the mining companies to focus on their core activities and to refuse taking over the responsibility for non-core activities such as the control and provision of social amenities that the ZCCM previously provided.[423] These measures considerably degraded the provision of these services to the mining community.[424] A failure to specify all the services that were provided by the ZCCM in the development agreements and to transfer the responsibility for these services to the private companies also contributed significantly to the lack of social responsibility of the mining companies (Fraser & Lungu, 2007:16, 17).

Higher healthcare fees and a decline in their standards under private ownership of the mines, and the closure of a number of the mine hospitals and clinics previously managed by the mines, reduced access to healthcare for the wider mining community, including the retrenched ZCCM mineworkers and their families. Before the privatisation of the mines, the mining community enjoyed easy access to these facilities. Under private ownership of the mines, these services were transferred to the government sector[425] or to Non-Governmental Organisations (NGOs) that lacked the budgets necessary for adequately maintaining many of these services (Fraser & Lungu, 2007:40, 50).[426] The most significant deterioration of health services was brought about by the dramatic collapse in preventative services, following the closing down of the public health departments by many of the successor mining companies (Fraser & Lungu, 2007:41).[427]

Passing the responsibility for the upkeep of mining townships (that before privatisation was 75% funded by the ZCCM) from the mining companies to the ill-resourced local

[423] Anglo American refused to take over some of the schools and hospitals previously run by the ZCCM and Metorex disposed of the school it took over when the company performed poorly.
[424] Interviews with Honourable Captain Moono, 2 December 2003 and Emmanuel Mutati, 18 November 2003.
[425] Via the District Health Management Boards (DHMBs).
[426] For instance, all three clinics in Kalulushi Township that the Chibuluma Mines handed over to DHMBs were forced to close down (Fraser & Lungu, 2007:40).
[427] On the other hand, except for NFCA that denies healthcare to all dependants of mineworkers, access to curative healthcare for permanent pensioned workers and their dependants in the ZCCM successor companies remained unchanged and, in most cases, is guaranteed in the development agreements (Fraser & Lungu, 2007:40, 50). However, while all workers that retired on medical grounds were given free medical support for life under government ownership of the ZCCM, under private ownership, those retired from the company would receive free access merely for 5 years and those made redundant were to receive 50% of their medical care only for one year (Fraser & Lungu, 2007:40).

municipal authorities, further degraded social services in Zambia. The private company now running the system is struggling to collect user fees leading to frequent suspensions in the provision of these services (Fraser & Lungu, 2007:36, 51). The introduction of user fees for the use of social amenities, subsequent to the separation of social and commercial amenities of the ZCCM during the privatisation process, alongside the removal of the subsidies that accompanied the economic stabilisation measures, also eroded the household income of the mining community. The mining community enjoyed these amenities free of charge before the ZCCM was privatised.[428]

The degrading of social services, alongside the huge retrenchments of mineworkers under private ownership of the mines, have added significantly to the huge reductions in Zambia's HDI and the enormous increases in poverty levels, despite the recovery of the mining industry, in more recent years. Section 4.4.5 of Chapter 4 shows that poverty levels increased from about 69.7% in 1991 under the Kaunda government to 73% in 1998 during the privatisation of the mines and when some of the mines were already under private ownership. These levels are even higher in rural areas (The Economist Intelligence Unit, 2008a:8). The high poverty levels under private ownership of the mines are also mirrored in the fall in Zambia's HDI by 0.17% annually between 1990 and 2007 from 0.495 to 0.481 (UNDP, 2009). However, Zambia's HDI dropped to its lowest level in 2000, after which it increased only marginally, despite the boom in copper prices from 2004 to 2006.

- *Shifting responsibilities for the treatment of pollution to the government*

The cost-reduction measure under private ownership that involved shifting some of the responsibilities for the treatment of mining pollution to the government (or to NGOs, who often lack adequate resources to competently address these), increased the cost burden of the Zambian government. It also contributed towards higher pollution levels from mining (Fraser & Lungu, 2007:33). The higher pollution levels are further significantly attributable to the ineffective policing of transgressions of pollution levels by the ECZ, despite its possessing the right to prosecute management or directors in

[428] Interview with John Kangwa, 21 November 2003.

their individual capacity, if upon investigation they have been found negligent in limiting or preventing pollution (Fraser & Lungu, 2007:37, 38).

- *Temporary closures and withdrawals*

Withdrawals of private mining companies from mining operations in Zambia to reduce losses or to maximise profits might potentially have a devastating impact on the development of the Zambian economy, manifesting the risks involved in the development of the host country when strategic assets are owned by *foreign* private companies (Africa Confidential, 2006:4). Additionally, the placement of RAMCOZ under receivership led to the unemployment of many miners and was at a huge cost to the government (elaborated upon in Section 6.1.3 of Chapter 6). Profit-maximisation measures that prompted some of the companies to suspend their operations also had a negative impact on employment and on production.

Metorex for example moved forward the development of the Chibuluma South mine and put on hold open-cast mining[429] and the processing of copper at their concentrator, in the latter part of 2001[430] and suspended its operations in March 2002 (Regulatory News Service, 2001; Times of Zambia, 2002, cited in Craig, 2002:365, 368).[431] Anglo American also deferred the development of Konkola Deep to cut its losses, before it withdrew from Zambia (Mining Journal, 2001, cited in Craig, 2002:365). Notwithstanding that the suspension of operations in the mines and the withdrawals from non-profitable operations prevalent under private ownership of the mines, might have been economically justified to reduce losses, such measures had an adverse impact on investment commitments of mining TNCs and on the development of Zambia.

The policy of some mining TNCs of reducing their shares in loss-making companies had a less negative impact on Zambia's economy than the closures of some of the mines and the withdrawal by a few mining TNCs. First Quantum addressed its poor performance at Mopani by reducing its interests in loss-making operations at the

429 To curb losses that the company experienced and following the lack of financial support.
430 Interview with Thomas Kabandama, 13 November 2003.
431 Until a substantial material improvement in the price of copper was to occur.

company, in 2003 from 44% to 16.9% (Table A5 in Annexure) while consolidating its capital into more profitable mining projects, such as its operations at Bwana Mkubwa, in which it had full ownership. Bwana Mkubwa enjoyed a profit of US$2.6 million in 2001 (World Bank, 2003b:132; Africa Mining Intelligence, 2002c:1; Regulatory News Service, 2001, cited in Craig, 2002:365). The low costs of production at Bwana Mkubwa were largely attributable to the low extraction costs of copper at the rich Lonshi mine in the Democratic Republic of Congo (DRC) that was processed in Zambia (World Bank, 2003b:132). However, Bwana Mkubwa that had a short lifespan was recently obliged to shut down its copper processing plant, causing the retrenchment of 365 workers (Bureau of Economic, Energy and Business Affairs, 2009).

- *Support foreign suppliers*

A reduction in the cost of production in the mines under private ownership was probably also achieved through mining companies' increasingly supporting foreign suppliers, claimed to be more price-competitive than Zambian suppliers (elaborated upon in Section 6.3.3.1 of Chapter 6). The practice of supporting foreign suppliers encouraged the de-industrialisation of the local industry, which has undermined the development of Zambia and is contrary to what was the case in developmental states. Under government ownership, the procurement and sales procedures of the ZCCM, designed to promote linkages to the local economy, albeit at a relatively small scale, increased the market for local suppliers to the mines and supported the few existing Zambian industries that supplied inputs to the mines (Fraser & Lungu, 2007:2, 10). However, higher procurement from local suppliers under government ownership was limited by the fact that the mining sector inputs comprised mainly of capital and intermediate goods that were largely absent in Zambia and were predominantly imported.

- *Depreciation of the kwacha*

The general decline in the value of the kwacha, which mining TNCs are able to manipulate through their effective control over Zambia's foreign exchange,[432] has contributed to a drop in the production cost of private mining companies, when local expenditure takes place in US cents per pound terms and is largely tax-deductible as well (Maambo, 1998:Fig. 9). While the alleged manipulation of the foreign exchange by foreign private mining companies to bring about a depreciation of the kwacha, would benefit the foreign private sector interests, a huge devaluation of the kwacha has a particularly harmful impact on the Zambian suppliers. This is mainly on account of consequent hikes in the prices of the highly import-dependent inputs of the manufacturing sector.

In summary, it is noted above that in the short-term several cost-cutting measures by the private TNCs imposed social and welfare costs on the Zambian economy and contributed to increases in poverty levels under private ownership.[433] The concessions granted to TNCs led to losses in government revenue. Accordingly, an evaluation of company performance exclusively on *x*-efficiency objectives provides only a partial picture.

A more balanced evaluation of the roles of private ownership of enterprises requires a weighing of the benefits of improved *x*-efficiency against the socio-economic costs of cost-cutting or profit-maximising measures on the Zambian society. The poor socio-economic impact of *x*-efficiency objectives on Zambia corresponds with the argument of Fine and Stoneman (1996:23) that an exclusive focus on *x*-efficiency objectives may even perpetuate unequal development, largely favouring foreign TNCs, legitimised in a market context. Greater redistribution of benefits from better performance of private mining companies especially through higher taxes, foreign currency earnings and the development of local capacities (also through higher employment) is necessary to promote development (elaborated in Section 6.3 of Chapter 6). Government measures, including negotiation with the private sector and a stronger implementation of

[432] Copper and cobalt contributed about 87.1% of Zambia's foreign exchange in 1993 that dropped to about 65.7% in 2000, at the time when all the mines were privatised (The Economist Intelligence Unit, 2002:39).
[433] In addition to among others HIV/AIDS, low economic growth and unsustainable debt servicing (The Economist Intelligence Unit, 2002:28).

regulations to ensure that greater benefits accrue to the Zambian nation under private ownership of the mines, are also crucial.

5.5 POLITICAL-ECONOMIC IMPLICATIONS OF THE PRIVATISATION AND PRIVATE OWNERSHIP OF THE MINES AND THE IMPACT ON DEVELOPMENT

The manner in which the privatisation of the mining sector proceeded had a highly unfavourable outcome on the political economy of most Zambians. Section 5.2.2 shows that several weaknesses in the institutional and regulatory framework and in the policies of the MMD government influencing the privatisation process facilitated corruption during the privatisation of the ZCCM. The major beneficiaries of the alleged corrupt and untransparent practices during the privatisation process were possibly the senior government officials who were said to be involved in the corruption of the mining sector immediately before the mines were privatised. The alleged corrupt practices likely deprived the Zambian economy of significant revenue that it otherwise would have been able to obtain from the privatisation of SOEs.

On the other hand, the failure to institute policies and laws that would have ensured more favourable outcomes for Zambians during the privatisation process and under private ownership of the mines, affected especially the mineworkers, the local suppliers and the Zambian economy in a negative fashion. In particular, omissions in the legislative and institutional measures to provide adequate social security and other safety nets to Zambian mineworkers that would have lessened the adverse consequences of privatisation, had a deleterious impact on the mineworkers during the privatisation process. The extensive retrenchment programme introduced in the mining sector immediately prior to the privatisation as demanded by the IMF and the World Bank, had a highly negative impact on the mineworkers and the mining community. Similarly to what was also the case with the privatisation of SOEs in Russia, the poorly executed privatisation contributed to decreases in income and increases in inequality (Stiglitz, 1998:19, 22, 2002:144, 157, 169).

Moreover, the above discussion shows that changes in ownership structure that introduced different manager objectives under government and private ownership altered the allocation of gains that brought about changes in the political-economic landscape of Zambia. It is noted from Section 4.3.2 of Chapter 4 that the electoral-maximising motives pertaining to state ownership, mainly during Kaunda's government, favoured the redistribution of gains from the extraction of the copper resources for the development of especially the Zambian mineworkers and of other non-mining sectors. These included increases in employment, significant development of the manufacturing sectors, improvements in the provision of social facilities to Zambians and Zambianisation policies. However, excessive spending of mining revenue, in the absence of a corresponding saving of a portion of mining revenue (to assist in cushioning the economy against the impact of lower copper prices) and of measures to improve the company's productive capacity (through capital and technology reinvestments), rendered these policies unsustainable. The over-extension of the revenue of the ZCCM into non-core mining sectors also hindered profit maximisation or better performance and contributed to the losses that the ZCCM experienced.

Conversely, Section 5.4.2 shows that certain cost-cutting and profit-maximising measures under the private ownership of the mines, would likely encourage improved company performance in the longer term, which would benefit mining TNCs. However, void of reviving the national economy, partly through redistributive measures, the practice of the private mining companies to allocate the returns from the extraction of copper resources mainly to themselves and their predominantly foreign shareholders, as discussed in Section 5.4.2, would not necessarily manifest in greater development for Zambia. This would especially be the case in the context where much of the profits are repatriated out of Zambia.

On the contrary, the subsidisation by the government of several activities of the mining companies, together with the high costs the mining TNCs imposed on the government greatly lowered government revenue. It is noted above that the transferring of costs occurred through the TNCs passing the responsibility for the provision of social services, the treatment of some of the pollution from mining and for the payments of part of the retrenchment and pension packages to the government. Additionally, the reduced accessibility of social services,[434] previously provided free of charge to the mining community by the ZCCM under government ownership,[435] eroded the welfare of the Zambian mineworkers and the mining community under private ownership of the mines.

Moreover, counter to the pro-worker policies of Kaunda's government under government ownership of the mines,[436] it is noted in Section 5.4.2 that several cost-reduction measures under private ownership of the mines had severe negative socio-economic ramifications in respect of the mineworkers and the mining community.[437] The social and welfare costs to the Zambian economy were mainly due to huge unemployment as a result of retrenchments, the substitution of local capacities with foreign capacities, the temporary closures of mining companies that are more frequent under private ownership and the withdrawals of some mining companies from Zambia. The eroding of the conditions of employment of workers and delays in paying out the retrenchment and pension packages of workers and significant reduction of these packages further affected workers adversely.

However, in the absence of growth through better performance of the mining companies, and of greater reinvestment into the more productive activities, such as the core mining sector, rather than mostly into the more unproductive sectors of the economy, the redistributive policies of the Kaunda government were rendered unsustainable. In addition, the de-industrialisation that the substitution of local suppliers by foreign suppliers encouraged and the decline in the value of the kwacha benefited the mining companies. However, these have a negative effect on the Zambian economy, in particular, the local suppliers and manufacturing base.

Besides some cost-reduction strategies of private mining companies, the poor capacity

434 Linked to the transfer of the responsibility for the provision of social services to the ill-resourced government.
435 Especially in education and basic health-care services (interview with Alick Lungu, 14 October 2003).
436 Encouraged by its electoral-maximising motives.
437 Interview with Charles Muchimba, 18 November 2003.

of the government also facilitated certain practices of private mining companies that had highly adverse consequences on local capacities and on the development of the country. The various deficiencies in government policies, institutions and laws governing the privatisation (elaborated upon in Section 5.2.2 above) and the activities of the private sector (refer to Section 6.5 of Chapter 6) have favoured the mining TNCs and the foreign backward-linked suppliers to the mining sector. The introduction of liberalisation policies before the mines were privatised further advantaged foreign suppliers. These weaknesses in government institutions and laws proved unsupportive to the local suppliers to the mining sector.

These political-economic outcomes of the privatisation and of profit-maximisation objectives and cost-cutting measures of private TNCs of the mining sector concur somewhat with Fine and Stoneman's (1996:19) argument that privatisation represents not merely a withdrawal of the state in favour of the market. Rather, it is a particular form of intervention which, depending on its form in immediate implementation and subsequent regulation, favours some capitalists, while disadvantaging others. The 'leaner' structures, generally promoted under private ownership and under market control, favour capital profitability, which is often foreign-based rather than domestically-based and discriminates against labour (Fine & Stoneman, 1996:23). Moreover, the limited growth and benefits for the mineworkers, local suppliers and the Zambian economy from the privatisation policies of the mines and under private ownership of the mines suggest that various qualifications are necessary to ensure more beneficial outcomes for Zambians from privatisation.

It can be concluded from the above discussion that electoral-maximising objectives of the government and certain state redistributive objectives could yield higher development outcomes, as was the case under Kaunda's government. However, when mining revenue became scarcer in the 1980s, the over-extension and the redistribution of mining resources into non-productive sectors at the expense of the core productive sectors of the economy became unsustainable. These policies then had an adverse impact on the performance of the mining sector and increased the debt burden of

Zambia that fed a further downward spiral of growth. The unsustainability of redistributive measures indicates that growth is also necessary for sustainable redistribution. However, not all states would necessarily pursue redistributive objectives.

For instance, the adoption of extensive privatisation and liberalisation policies during Chiluba's government greatly reduced the capacity of the government to influence decision-making in the mining sector. The lower government capacity, alongside the strict SAPs that the IMF and the World Bank imposed on the Chiluba government that limited government expenditure, and the corruption that allegedly prevailed under Chiluba's government, hindered greater redistribution of gains from the privatisation and the private ownership of the mines. In contrast, the nationalisation of the mines and political interests introduced into the mining sector under Kaunda's government enhanced the state's capacity to influence decisions in the sector.

On the other hand, improved *x*-efficiency of private mining companies would likely augment growth in Zambia's mining companies. However, several of the profit-maximising and cost-cutting measures of mining TNCs would not necessarily translate into higher development for Zambia. In the absence of a greater and more equitable redistribution of mining surpluses these measures, together with certain weaknesses in government institutions and laws regulating the privatisation and the private ownership of the mines, exacerbated inequalities in Zambia and undermined Zambian capacities. These outcomes blocked rather than promote development in Zambia, partly reflected in steep increases in the poverty levels in Zambia, following the privatisation and the private ownership of the mines.

Accordingly, development is a function not only of the performance of the mining companies but also of adequate redistribution of returns from mining resources to improve equity. In addition to growth in the company, development also requires inter alia, improvements in production levels, government revenue, permanent employment levels, human capital development, the development of local suppliers, as well as reductions in poverty levels. Sustainable and more equitable development needs a correct balance between growth and the redistribution of an appropriate proportion of surpluses from the mining companies to the Zambian economy.

CHAPTER 6

6. THE ROLES OF TNCs IN THE MINING SECTOR OF ZAMBIA WITHIN A WEAK STATE

This chapter addresses the research question as to the impact of the activities of mining TNCs on the development of the mining sector and the Zambian economy. Key components of the investigation are the investment and capital inputs from mining TNCs, the returns to the Zambian economy from the extraction of minerals and the role of the government in influencing the activities of mining TNCs.

The roles of TNCs in the mining sector in Zambia, within a weak state, are assessed first by examining their contribution in exploiting the unused resources of the copper mining sector and in supplementing the technology and capital of Zambia. Second, the main consequences of the dominant bargaining position of the mining TNCs over the government on the Zambian economy are considered. Third, the returns to the Zambian economy from the extraction of copper are investigated. Fourth, the factors that influenced the decisions of Anglo American and AVMIN to depart from Zambia are explored. This is followed by an assessment of the political economic implications of: (i) the regulatory and institutional capacities of the government in controlling the activities of mining TNCs; and (ii) the activities of TNCs in the mining sector.

6.1 THE ROLES OF TNCs IN EXPLOITING UNUSED MINING RESOURCES AND IN SUPPLEMENTING ZAMBIA's TECHNOLOGY AND CAPITAL

This section reviews the roles of mining TNCs in exploiting the mineral resources of Zambia and in supplementing the technology and capital of the mining sector in Zambia. The activities of Binani in the mining sector are then assessed as a case study to further evaluate the role of TNCs in supplementing the resources of Zambia. The findings would test the validity of arguments of neo-classical and neo-fundamentalist theorists that TNCs generate and supplement the resources of host countries and the contrasting views of neo-imperialists and Global Reach theorists that certain activities of TNCs subvert the development of these countries.

6.1.1 The roles of TNCs in exploiting mining resources

The mining TNCs invested significant capital into the mining sector compared to immediately before the mines were privatised. The crippling financial constraints that the government sustained were largely responsible for the lack of investments from the mid 1990s under government ownership of the mines. Investments in prospecting and exploration activities that peaked at US$5.2 billion in 1997, the re-opening of unused mines and the opening of new mines, enabled greater exploitation of Zambia's mining resources. Subsequently, exploration activities declined by almost 58% in 2001 below the peak exploration spending of 1997 to about US$2.9 billion, and by almost 15% from its 2000 level (Maambo, 1998:Fig. 13; Africa Research Bulletin, 2001d:14978). Table A8 (in Annexure), lists some of the exploration and prospecting activities of various mining TNCs in Zambia, including TNCs that did not acquire ownership of any mines.

The financial investments of the mining TNCs, in the late 1990s, enabled the re-opening of Chambishi Non-Ferrous Metals, the Chibuluma mines, Kansanshi and Bwana Mkubwa that were closed in the late 1980s and early 1990s (Lungu, 2001:16; Fraser & Lungu, 2007:48). Financial investments at Chambishi Non-Ferrous Metals to refurbish and upgrade the equipment and infrastructure of the mines and the concentrator extended the life of the mine since the company commenced the production of copper in 2003 (Fraser & Lungu, 2007:48; The Economist Intelligence Unit, 2007b:36). Furthermore, J and W planned to spend over US$200 million to develop the Muliashi mine[438] that was abandoned in the 1990s and to upgrade operations at the Baluba copper mine (The Economist Intelligence Unit, 2007b:36).

Major new mining developments that hold significant potential for considerably expanding the mining resource base of Zambia include the exploiting of the largely untapped, lucratively resourced Lumwana Copper Mines,[439] developed by Equinox Resources,[440] and the KDMP that contains the largest copper resource in the Copperbelt (The Economist Intelligence Unit, 2007b:35). The KDMP is being developed by

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[438] Benny Steinmetz Global Resource Group, a renowned diamond trader, is in partnership with J and W in Muliashi and their joint venture is named ENYA (Africa Mining Intelligence, 2006a:3).
[439] That was expected to start producing 165 000 tons of copper per annum, from 2008.
[440] A Canadian-listed mining company.

Vedanta Resources (The Economist Intelligence Unit, 2007b:35; Africa Mining Intelligence, 2002d:4). Furthermore, the expansion of Kansanshi under the majority ownership of First Quantum,[441] at a development cost of US$290 million,[442] would raise the lifespan of the mines to 30-40 years (The Economist Intelligence Unit, 2007b:36; Martin Creamers Weekly Online, 2003a). Both the unused mines that were re-opened and the new mining developments would increase mining production.[443]

6.1.2 The roles of TNCs in supplementing technology and capital

The mining TNCs also increased the technology and capital stock of the copper mines in Zambia from the immediate pre-privatisation levels. These investments are expected to have a highly positive impact on the development of the mining sector. Immediately prior to the privatisation of the mines in the late 1990s, insufficient reinvestment into the mines mainly due to lack of resources was the single most important reason for the poor performance of the mining sector under government ownership.[444]

Key considerations in the assessment of the contributions of mining TNCs to the technology and capital of the host country are (i) the size of investments; (ii) factors influencing the investment levels; (iii) the origins of the capital; (iv) the ability of the government to achieve similar investment levels under government ownership of the mines; and (v) the impact of greater efficiency of TNCs[445] in promoting higher investments in the mines than under government ownership.

(i) <u>Size of investments</u>

With the exception of Binani, the mining TNCs played a pivotal role in transferring additional technology inputs and capital stock into the mining sector of Zambia. Tables A5 and A9 (in Annexure) respectively list the technology and capital inputs that the

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[441] First Quantum also owns the Bwana Mkubwa Mines, the MCM (in partnership with Glencore), the Lonshi copper mine, as well as the Chambishi smelter (not the same smelter as the one that the Chinese Non-Metal Ferrous Company is establishing, also in Chambishi), where it processes large deposits of copper and cobalt from the Lonshi Mines, located in neighbouring Congo-Kinshasa (Africa Confidential, 2006:4).

[442] The incapacity of the design output to accommodate the production at the Kansanshi Mine from the first phase, commissioned in early 2005, led to the expansion of the mine, with the prospect also of finding gold (Africa Confidential, 2006:4).

[443] Production of copper at Kansanshi was expected to increase from 127 000 tons in 2006 to 165 000 tons in 2008.

[444] Interviews with David Chilipamushi, 17 December 2001; Danny Kalyalya, 14 December 2001; Alick Lungu, 20 December, 2001; Norman Mbazima, 18 December 2001; Willie Sweta, 15 December 2001.

[445] Owing to their expertise, technology and private sector investment.

major mining companies pledged for the existing mines in Zambia and some of the most significant technological and capital inputs that TNCs actually invested in the Zambian mining sector. These inputs reinvigorated the mining industry and contributed to the rise in copper production levels (Fraser & Lungu, 2007:1, 19). Foreign investment in the mining sector for refurbishing the plants and for the purchase of spares and machinery is estimated at nearly US$4 billion[446] from 2000 to 2007 (The Economist Intelligence Unit, 2008b:19, 35; Fraser & Lungu, 2007:19). The rise in real gross fixed capital formation to an estimated 19% of GDP in 2006 and to around 25% in 2007 from only 13.5% in 1990 and 11% in 1994, primarily reflected the new investments in the mining sector (The Economist Intelligence Unit, 2002:35, 2007b:26, 2008b:15).

However, despite substantial capital that the TNCs ploughed in the mines, in the short term these investments were generally less than they had pledged in the development agreements and took place mainly during the boom from 2005-2007 (Transparency International, 2002:6). For instance, the total of US$590 million that the three largest mining companies invested by 2000, fell short of the approximately US$822 million expected in committed investments from privatised mining companies that were required to re-engineer, recapitalise and to modernise existing operations (World Bank, 2002b:17; ZPA, 2000b:15). Moreover, the mining TNCs failed to contribute the US$1 billion by 2000 that was expected as contingent investment, mainly for the implementation of greenfield projects and for expansions during the first ten years (ZPA, 2000b:15).

The Chamber of Mines' own figures show that the investment of the ZCCM in the copper mines, in the last seven years before the mines were privatised, 1990-1996, of around US$125 million a year, was not significantly lower than the average investment levels of around US$135 million a year achieved in the first seven years, from 1997-2003, under private ownership (refer to Figure 4.11 of Chapter 4) (Fraser & Lungu,

[446] The MUZ provides a much lower investment estimate of US$1.4 billion, from 1998 to 2006, against that of The Economist Intelligence Unit. The significant investment that occurred in 2006-07, mainly due to high copper prices, would perhaps augment this figure somewhat, albeit less than The Economist Intelligence Unit suggests.

2007:20). In fact, if the effect of inflation on the US dollar is taken into account, the investment levels from 1997-2003 declined in real terms from the average investment levels between 1990 and 1996, under government ownership.

(ii) Factors influencing investment levels

Notwithstanding that the mining TNCs introduced major investments in sums that were unavailable to the ZCCM, it is unclear whether the higher investments in mining and the opening of the new mines came about solely as a result of private TNCs' ownership of the mines. A closer examination of the investment trends shows that significant investments from the mining TNCs only began in 2004, at the start of the international copper price boom and increased especially in 2006, when copper prices peaked at unprecedented levels.[447] This indicates that the dramatic increases in the price of copper were highly significant in influencing the investment levels in mining.

A major contributing factor for the lower investment levels in the mining sector than were pledged was likely the practice of TNCs of delaying investment in the short term to enable them to first gauge whether the venture merited greater investments. As is noted in Section 4.4.10 of Chapter 4, this supports the 'real options view of investment', based on the assumption of irreversible investment costs, the uncertainty of future pay-offs and of future output prices that encourages investors to postpone their investments[448] (Dixit & Pindyck, 1994, cited in Andersson, 2000:79). It further confirms the observation of Andersson (2000:79) that the real options approach is highly relevant in the African context. Conversely, the delay in investments of mining companies contradicts the neo-classical model of investment of Jorgenson (1963), which states that the firm chooses its capital stock so as to maximise the present value of the future cash flow, assumed to be known with certainty. This theory assumes that the firm can sell the excess capital without a loss; that is, the firm chooses their capital stock to equalise the marginal product of capital with the user cost of capital (cited in Andersson, 2000:79).

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[447] In the period 2000-2003, the average copper price on the LME varied from US$1 558 per ton to US$1 815 per ton, which doubled over the next two years to US$3 684 per ton (Fraser & Lungu, 2007:20).

[448] The greater the uncertainty and the higher the value of the potential investment, the greater would be the likelihood that the firm would postpone the investment decision (Andersson, 2000:79). Possible investments that foreign companies possess elsewhere would likely mitigate losses in returns that they might incur from the postponements.

The bid design, allowing for pledged investments rather than specific investments, that enable TNCs to delay their investment commitments, also precluded higher investment from mining TNCs. It further facilitated Anglo American's departure from Zambia before honouring all its investment obligations. Additionally, a dependence on existing mining operations to fund greenfield projects contributed considerably to the lower capital and technology investments received from some mining TNCs.[449] This practice further undermined the development of new mines in instances when the existing mines under-performed. For instance, the failure of Metorex to obtain the expected cash flows from production at Chibuluma West that were planned to fund capital expenditure at Chibuluma South,[450] led to the temporary suspension of operations at the Chibuluma South mine[451] in September 2001 (Regulatory News Service, 2001; Times of Zambia, 2002, cited in Craig, 2002:365, 368; Chibuluma Mines plc, 2003:3; The Economist Intelligence Unit, 2002:42; Engineering and Mining Journal, 1998:14).

Moreover, the losses that KCM experienced for most of the time prevented it from funding new projects. Furthermore, these losses alongside the company's inability to raise US$313 million of limited recourse finance, accounted significantly for the failure of the Anglo American consortium to respect their investment pledges. These pledges included an investment of US$208 million in capital expenditure (capex); the turning around of the old Konkola and Nchanga mines within three years of their operation; and an investment of a further US$523 million in the greenfield project, the KDMP[452] (refer to Table A5, in Appendix) (Mining Journal, 2001, cited in Craig, 2002:365; Ministry of Finance and Economic Development, 2000:62; Engineering and Mining Journal, 2000b:11, 16). Various weaknesses in government policies, discussed in Section 6.5.1, further account for the lower investment levels of mining TNCs in Zambia in the short

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449 Interview with Jack Jones, 22 October 2003.
450 Which has an approximate life of 14 years.
451 Until the price of copper improved, or until additional funding was sourced. An agreement reached with the IDC, of South Africa, to provide equity-based funding for the Chibuluma South underground project in 2003 solved the funding problem that Metorex experienced at the time (Chibuluma Mines plc, 2003:3).
452 The Konkola Deep, one of the biggest copper ore bodies in the world, was ZCCM's main greenfield development project near the operational Konkola mine, with an estimated reserve of between 400 and 500 million tons, at 3.8% copper, and a productive capacity of over 200 000 tons/year and substantial tonnages of cobalt. However, the mine, which is one of the wettest in the world, required US$1billion in fresh investment by 2002 (The Economist Intelligence Unit, 2002:40; Kaunda, 2002:81, 186).

term.

(iii) The origins of capital

The origins of the capital from TNCs, namely local or international, also significantly influenced the benefits to the host country from the participation of TNCs. It has been shown above that the failure of several mining TNCs to bring in adequate funds raised outside Zambia (in the expectation that the mines would largely finance themselves), limited the capital contributions that potentially pertain to mining TNCs. Moreover, the reliance of mining TNCs on existing mining operations that they owned in Zambia for funding new projects diminished the potential benefits of capital and technology transfers at a low cost to the host country that neo-classical theorists and neo-fundamentalists attribute to TNCs. Additionally, the borrowings of Binani from the Zambian state-owned bank[453] and much of which were not paid back (discussed in Section 6.1.3) represented a drain on Zambia's resources.

(iv) The ability of the government to achieve high investment levels

Notwithstanding that the TNCs invested less than what they had pledged, the capital and technology stock of Zambia improved under TNCs' ownership of the mines. In the 1990s, the high debt of the country and the poor performance of the ZCCM left the government with insufficient resources required to adequately reinvest in the mines. The tendency of the government to divert revenue from the mining sector (as the cash cow of the Zambian economy) for fulfilling multiple objectives and electoral-maximising motives, has also reduced the resources available for reinvestment in the mines. This was especially the case in the latter part of Kaunda's government, discussed in Section 5.4.1.1 of Chapter 5.

The constraints that demand management programmes of the SAPs placed on government spending in the 1990s limited to some extent the redistributive leverage of the Chiluba administration. Rather, the lack of resources, linked mainly to the poor performance of the mining sector in the 1990s under government ownership, the historic

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[453] To pay, among other things, the retrenchment packages of the workers at RAMCOZ.

low copper prices and the prolonged economic downturn, contributed more significantly to the low investment levels in the 1990s (Fraser & Lungu, 2007:19; The Economist Intelligence Unit, 2007b:27). Furthermore, insufficient reinvestment into the mining sector, especially in the 1990s, was not necessarily only because of government ownership. In particular, IMF and World Bank policies barring greater government investment into the mines that were earmarked for privatisation from 1996 were also greatly responsible for the large reductions in investments in the mines in the 1990s under government ownership. In turn, the inadequate investment into the mines reinforced the cycle of poor performance and lower revenue from mining available for reinvestment in the mines.

Moreover, the large-scale technological investment in the tailings leach plant[454] established in 1974 in fact occurred under government ownership and management control of the mines.[455] The plant was the largest of its kind in the world, and at the time placed Zambia at the forefront of the development of the solvent extraction process. However, these developments coincided with a time when resources were more readily available (Maambo, 1998:5). At times of low government revenue the state was unable to adequately recapitalise the mines. This underscores the important role that TNCs could play in building the technology of host countries that face significant financial constraints.

(v) <u>Impact of greater efficiency of TNCs in promoting higher investments in the mines</u>

Presumably, higher efficiency achieved under private ownership of the mines by TNCs, and their greater expertise and access to technology would raise revenue from the mining sector that could also be used for reinvestment in the mines. However, difficulties in obtaining information on the performance of private mining TNCs and the relative short term that the mines are under TNCs' ownership render it not possible within the scope of the study to definitively determine a correlation between company performance under private TNCs' ownership of the mines and investment levels.

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454 Interview with Norman Mbazima, 18 December 2001.

455 Whereby low-grade material could be leached and the resultant low tenor liquors upgraded.

Nonetheless, better performance under private ownership of the mines might not necessarily be expressed in higher investment levels. For instance, the 'wait and see' attitude of mining TNCs, discussed above, likely limited higher investment in the short term. However, in the medium term, the general better performance of the mining sector, mainly owing to the high increase in the copper price, did result in a significant rise in the technological and capital investments in the mining sector.

Benefits of higher investments by mining TNCs would further diminish if a large portion of the rent element from mining is repatriated out of Zambia under private ownership of the mines by TNCs. Investment therefore also needs to be assessed against the repatriation of mining profits out of Zambia, to determine whether the activities of TNCs amount to a net inflow of resources. However, difficulties in detecting transfer pricing policies of mining companies and because of the unavailability of reliable data, render such an investigation outside the scope of the study.

Accordingly, the level of investment seems less a function of ownership than of resources available for investment and of other factors that impinge on performance. However, in the context of the poor performance of the mining sector and the Zambian economy and a highly indebted government, the role of TNCs as significant potential conduits of capital and technology for developing countries was pivotal in augmenting sorely needed investments for the mining sector in Zambia. The poor bargaining leverage of the government compared to the mining TNCs in Zambia and certain weaknesses in the institutional, regulatory and implementation capacity of the government to enforce investment commitments of TNCs, elaborated upon in Section 6.5.1, also limit the extent of the technological and capital transfers from TNCs to the mining sector.

6.1.3 Activities of Binani: a case study

Measures that Binani undertook to limit its losses and their impact on the economy are examined below to further investigate the argument that TNCs are significant conduits of capital and technological investment. In particular, the investigation focuses on

Binani's failure to repay bank loans and pay suppliers, workers and statutory bodies,[456] and its stripping of the mining assets from Zambia. This is followed by a consideration of the government's assumption of the role of the receiver of RAMCOZ and the consequences on the economy.

(i) Liabilities to the banks

Binani failed to pay back its liability of K13.7 billion to the Zambian state-owned bank, the Zambian National Commercial Bank (ZANACO), obtained at government instruction[457] and to pay the retrenchment packages of workers. This contributed to ZANACO incurring a loss totalling at least US$150 million in non-performing loans in the latter part of Chiluba's presidency. The loss was significantly to blame[458] for the subsequent financial difficulties that the bank experienced (The Economist Intelligence Unit, 2002:44; Committee on Economic Affairs and Labour, 2000:54, 61, 62, 112).[459] The financial difficulties of ZANACO forced the government to issue bonds worth K250 billion to recapitalise the bank, to cover the liabilities to the bank of both Binani and Zambia National Oil Company (ZNOC) and the contingent liabilities of legal action by some ex-employees of ZANACO (Government of Zambia, 2002:paragraph 22). The poor performance of ZANACO during this time also led to the IMF's demand that the bank privatise about 49% of its shares.[460]

The failure of Binani to pay back loans borrowed from local banks supports the arguments of Helleiner (1989:1455) that when DFI is largely achieved through borrowing from a local bank, national gains in the supply of capital and foreign exchange would be unlikely. Moreover, if the capital that TNCs borrowed from the local banks is not effectively invested within the host country, which was the case with Binani, net gains in the supply of capital and foreign exchange from TNCs would be unlikely and the borrowing amounts to a capital outflow (Helleiner, 1989:1455). Furthermore, the risks that the activities of Binani introduced to the viability of

456 Interviews with Zion Simwanza, December 2003 and John Lungu, 12 November 2003.
457 The Chiluba government's acceptance of RAMCOZ's high debt levels reflects gross negligence on the part of government in the protection of public funds.
458 Together with the liabilities of the ZNOC.
459 Interview with Ladslous Mwansa, 13 December 2001.
460 Interview with Ladslous Mwansa, 7 October 2003.

ZANACO, also affirm the neo-imperialists and the Radical Dependence School's argument that TNCs introduce risks to the host country (Helleiner, 1989:1454; Padayachee, 1995:164).

(ii) Liabilities to suppliers

The massive debts of Binani to suppliers, in particular the debt of US$20 million to the Copperbelt Energy Corporation (CEC) and its debt to the Zambian Railways,[461] and delays of up to six months in paying its suppliers, considerably degraded the earnings of the suppliers.[462] The debts were detrimental to local suppliers and to the development of Zambia's backward-linked industries. This was especially in light of the dramatic depreciation of the kwacha, by 194% from 1997 to 2000, an average inflation rate of about 25.4% from 1997 to 2000 and of the high bank interest rate charges, ranging from 46.7% to 31.8% on short-term borrowing from 1997 to 1998 (Africa Mining Intelligence, 2003a:2; Engineering and Mining Journal, 2000c:26; Catholic Secretariat, 2001:13).[463] State assurances and guarantees forced the government to pay the liabilities of Binani owed to CEC.

(iii) Failure to fulfil commitments to workers

Several policies of Binani also affected workers adversely. These encompassed the failure of Binani to fulfil its commitments to retain the full labour force of about 7 000 that it inherited, to apply the normal retirement benefits to those who wanted to retire, and to pay the termination and retrenchment benefits[464] of many workers during the receivership of RAMCOZ. The company further delayed paying salaries of workers (Lungu, 2001:15). The government decided to take over, among several other liabilities,[465] the responsibility for paying both the terminal benefits of the employees that RAMCOZ failed to honour and the remuneration of the employees of the

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[461] Interview with Simon Capper, 30 October 2003.

[462] These difficulties include several of its suppliers being unable to pay VAT that the ZRA requires within a month following their submissions (interview with Eddy Kapungulya, 13 November 2003).

[463] Interview with Eddy Kapungulya, 13 November 2003.

[464] An excess staff of 2 000 workers was initially retrenched on the advice of an industrial engineering review, which concluded that a workforce of only 3 965 employees were required for rational operations at Luanshya/Baluba (Kaunda, 2002:55, 56, 180). A further 1 000 workers were laid off after the initial retrenchment (interview with John Lungu, 12 November 2003). A technical assessment of the pre-bid studies, which deemed this commitment unrealistic, also assessed that about 3 000 retrenchments would be required (World Bank, 2002b:21). ZCCM also found that operations at Luanshya/Baluba mines could not sustain the level of employment (ZPA, 2003:2).

[465] Interview with Ladslous Mwansa, 7 October 2003.

company.[466]

The remuneration of employees was partly achieved from an unauthorised payment of about US$5 million from the HIPC fund, in 2002, which the government had to reimburse (World Bank, 2002b:7, 16, 20, 23). Between 2000 and 2002, also during receivership, the mineworkers of the Luanshya/Baluba mines were not paid their termination and retrenchment benefits (World Bank, 2002b:20). The dramatic increases in unemployment levels, owing to the high retrenchments of workers and the closure of some suppliers in the region, partly as a result of Binani delaying or absconding from paying local suppliers for services rendered, had a particularly harmful impact on the economic life of Luanshya (World Bank, 2002a:11; Catholic Secretariat, 2001:14; CCJDP, 2002b:10; Lungu, 2001:6).

(iv) Failure to pay statutory bodies

The failure of Binani to pay back its debt commitments to statutory bodies and its omission to timeously remit the workers' contributions to the Mukuba Pension Scheme were a further significant cost to the country. It also contributed to a collapse of the social services in the area, leading to labour unrest. The statutory bodies that Binani did not pay included the ZNFP, Zambia Electricity Supply Corporation (ZESCO), ZCCM, ZRA and the Luanshya Municipal Council (GRZ, cited in Committee on Economic Affairs and Labour, 2000:54, 61, 62, 112; Catholic Secretariat, 2001:13; Africa Mining Intelligence, 2003a:2; Transparency International, 2002:1, 23, 24).

(v) Asset stripping

Rather than supplementing the technology and capital of Zambia, Binani also stripped the productive assets of RAMCOZ and repatriated the money received from the assets out of the country. This was achieved by way of dismantling and selling the machinery and equipment of the smelter at Luanshya that were transferred out of Zambia, ostensibly for servicing, but that were not returned (World Bank, 2002b:13; Catholic

[466] Interview with David Chilipamushi, 20 October 2003.

Secretariat, 2001:14).[467] The subsequent further dismantling of the remaining parts of the smelter by the receiver, to enable it to pay the liabilities of Binani, led to the complete eradication of the smelter at Luanshya.[468] RAMCOZ-Ndola Precious Metals also collapsed at the beginning of 1999, owing to the problems that the Binani Group, its holding company, experienced (World Bank, 2002b:13).

(vi) <u>RAMCOZ under receivership</u>

The government's assumption of the role of the receiver of RAMCOZ,[469] through its position as the major creditor or debenture holder of ZANACO, also imposed very high liabilities on the government. Inadequate and inappropriate government measures to effectively deal with the prolonged receivership and the liquidation of RAMCOZ (mostly because of difficulties experienced in finding an appropriate investor)[470] under care and maintenance were also at great expense to the government.[471] In particular, the high electricity bill, mainly owing to pumping activities to prevent the flooding of the mines[472] contributed significantly to the huge costs that the government incurred under receivership.

Additionally, a failure of the government to adequately de-water the Luanshya underground mine (that possessed good copper ore grades) under care and maintenance[473] resulted in the mines being flooded. The mines were still flooded at the end of 2006, reducing investor interest in the Luanshya mines.[474] This led to the new owners of the Luanshya Copper Mine (LCM[475]), upon determining that the Luanshya underground copper mines would be unprofitable, seeking permission from the government to close the Luanshya mine (Africa Mining Intelligence, 2006b:2).[476] The

[467] Interviews with John Lungu, 12 November 2003 and Simon Capper, 30 October 2003.

[468] Which would force the new owner, J and W Holdings, to smelt its concentrates at the smelter in Kitwe (interview with John Lungu, 12 November 2003).

[469] Interviews with Fortune Kamusaki, 25 November 2003; Fred M'muembe, 14 October 2003 and Zion Simwanza, December 2003.

[470] Interviews with Bernadette Mwakacheya, 17 October 2003 and Willie Sweta, 30 October 2003.

[471] Interview with Simon Capper, 30 October 2003.

[472] Interview with Ohene Nyanin, 29 November 2003.

[473] Interviews with Gilbert Temba, 13 October 2003 and John Lungu, 12 November 2003.

[474] Interviews with Silane Mwenechanya, 24 October 2003 and John Lungu, 12 November 2003.

[475] An affiliate of the J and W group that was awarded the mines after RAMCOZ left.

[476] Subsequently, the Zambian government also cancelled the exploration license rights of Puku Minerals (a wholly-owned affiliate of Weatherly International plc) to re-open the Luanshya underground copper mine. The cancellation of the licence of Puku minerals, subsequent to the government already having awarded it the exploration permit and after Weatherly had already raised

Baluba section, the most profitable part of the Luanshya mine, was not affected by the flooding.[477]

Delays in paying suppliers to the mines during the receivership and the liquidation process of RAMCOZ[478] also had an adverse influence on the suppliers of the mines.[479] The delay in particular jeopardised the activities of ZESCO, the power company of Zambia, whose liquidity problems were eventually resolved through various debt swop arrangements between itself and the government.[480] Moreover, mining companies that previously obtained acid (an important and one of the most expensive input requirements of mining companies) from the Baluba Mines, owned by RAMCOZ, were forced to import additional acid from Zimbabwe and South Africa.[481]

Under receivership, the government also paid both the salaries of the residual employees at RAMCOZ,[482] and the terminal benefit of 4 000 workers that had to be retrenched, with the mine being placed under receivership (World Bank, 2002b:20; CCJDP, 2002b:11). At the end of 2003, the government raised US$35 million to cover the terminal benefits and salary arrears of these employees (Times of Zambia, 2003:1). The delay in the payment of accumulated or terminal benefits and other liabilities to workers as unsecured creditors[483] had a highly negative impact on their well-being (World Bank, 2002b:14, 16; Committee on Economic Affairs and Labour, in Catholic Secretariat, 2001:13; CCJDP, 2002b:10, 11).

It is noted from the above discussion that the borrowing activities of Binani from the national bank, ZANACO and the failure to pay its liabilities to the bank, suppliers, workers and statutory bodies in Zambia, for which the Zambian government had largely

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US$7 million for the development of the project and US$10 million for drilling work and a feasibility study, prompted the company to take legal action against the government (Africa Mining Intelligence, 2006b:2).

477 Interview with John Lungu, 12 November 2003.

478 Interview with Eddy Kapungulya, 13 November 2003.

479 On account of the receiver, ZANACO, first recovering money owed to itself before considering money that RAMCOZ owed to local suppliers.

480 Interview with Ohene Nyanin, 29 November 2003.

481 Interviews with Danny Kalyalya, 14 December 2001; Norman Mbazima, 18 December 2001 and Willie Sweta, 15 December 2001.

482 Since many workers that were not retrenched were still entitled to salaries, despite operations being halted for several months at the Luanshya/Baluba mines (interviews with John Lungu, 12 November 2003; Bernadette Mwakacheya, 17 October 2003; and David Chilipamushi, 20 October 2003).

483 Interview with Danny Kalyalya, 31 October 2003.

assumed responsibility, and the asset-stripping activities of Binani at RAMCOZ were a great cost to the Zambian nation. The government's subsequent assumption of the role of receiver of RAMCOZ was also at a substantial loss to the state coffers. These practices of Binani in Zambia contradict the neo-classical and neo-fundamentalists' view that TNCs generate resources and supplement the technology and capital of the host country. Rather, the activities of Binani support the argument of neo-imperialists and Global Reach theorists that TNCs subvert development and promote the 'underdevelopment' of host countries, partly by draining the resources of the host country.

However, not all the mining TNCs in Zambia followed Binani's rather parasitic example as most made considerable investments in Zambia (noted above, in Sections 6.1.1 and 6.1.2). The greater exploitation of Zambia's resources and the technological and capital inputs of virtually all of the mining TNCs into the Zambian mines support the supplement and resource generation assumptions that neo-classical theorists[484] and neo-fundamentalists[485] ascribe to TNCs. Furthermore, the poor bargaining leverage of the government also abetted many of the negative actions of Binani.

The government's inability to force Binani to pay its liabilities in Zambia and the instruction of the Chiluba government that the national bank grants loans to Binani proved grossly negligent. Moreover, as is observed above, the decision of the government to assume the liabilities of Binani was at a great expense to the Zambian economy. An alleged corrupt relationship that the Chiluba government had with Binani probably also encouraged some of the actions of the mining company.

6.2 MAIN CONSEQUENCES OF THE DOMINANT BARGAINING POSITION OF MINING TNCs OVER THE GOVERNMENT

As is noted in Chapter 3, a strong bargaining position of the government is necessary to ensure that the greatest possible share of the rent element from mining accrues to the government, which is crucial to maximise gains in economies dominated by an

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[484] Vernon (1979, cited in Buckley, 1985:8).
[485] Warren (1980, cited in Jenkins, 1987:19, 31 and 32).

exhaustible resource (Chang, 1998:238). The argument of proponents of bargaining that governments possess great influence in extracting favourable gains from the activities of TNCs in their countries, through bargaining with TNCs, are gauged against an unequal bargaining relationship in which TNCs enjoy a dominant role over the government.

The poor bargaining leverage of the Zambian government was mainly owing to: donor pressure; various trade agreements that curtailed industrial policies of the government; Zambia's poor economic position, especially its foreign exchange problems; practices of TNCs to co-ordinate and to consolidate their power; some corrupt practices; and weaknesses in the capacities of the state. In contrast, the various pressures that the Zambian government faced increased the leverage of the TNCs, especially of Anglo American,[486] over that of the government during the privatisation of the final assets of the ZCCM. Table A6 (in Annexure) lists in detail the various factors that reduced the bargaining leverage of the Zambian government.

The consequences of the dominant bargaining relation of the mining TNCs over the government are investigated below by examining the outcomes of the collaboration of some TNCs through the Kafue Consortium in the bidding process in the privatisation of the mines. This is followed by an investigation of concessions granted to the privatised mining TNCs.

6.2.1 The Kafue Consortium: a case study of the behaviour of TNCs collaborating for a dominant bargaining position in the bidding process

The operations of the Kafue consortium during the bidding process for the final assets of the ZCCM represent an appropriate case study of the behaviour of TNCs in a dominant bargaining position with the government in the privatisation of SOEs. The formation of the Kafue Consortium in 1997-98, comprising of companies that pre-qualified before as single entities in the bid for the 'Aco' package,[487] likely represented a deliberate strategy to increase the consortium's bargaining power over that of the

[486] That possesses considerable bargaining leverage, through its experience in negotiating deals to maximise their gains and to protect themselves.

[487] The final and most lucrative assets of the ZCCM, encompassing the Nkana and the Nchanga Divisions and the Chambishi Acid and Cobalt Plants.

Zambian government and to reduce competition during the bidding process (Transparency International, 2002:22). Alongside a weak government, the reduced competition enabled the Kafue Consortium, as the only entity to bid for the 'Aco' package, to undervalue the assets of the ZCCM it was to gain during the negotiations.

The discounted cash flow method that was adopted that the ZPA and the foreign advisors favoured for calculating the value of the mines, largely based on the price the buyer is prepared to pay through competitive bidding, encouraged the buyers to undervalue the mines. The discounted cash flow method factored in its calculations of the value of the mines the investment inputs from the bidder to improve the existing assets, the price of copper and the time it would take for investors to recoup their investments.[488] Accordingly, the profit-generating potential of the business (based on existing market conditions) largely determined the price in the discounted cash flow method,[489] favouring the buyers at the expense of the sellers, according to Kaunda (2002:168, 169). This differed from an asset-based value of the mines, whereby the market value of the assets of the ZCCM was to serve as a guide in setting the price for the mines.[490] The ZPA and foreign advisors felt that an asset-based value of the mines had a limited bearing on the actual value of the enterprise,[491] since the assets might not always bring in an income for the buyer (ZPA, 2003:6; Kaunda, 2002:169).

The undervaluing of the assets of the ZCCM by the Kafue Consortium was orchestrated by putting little value on the underground mines,[492] placing no value on some assets they were to acquire[493] and by overvaluing their expenditure. The considerable sums that the individual members of the Kafue Consortium, subsequent to its dissolution, bid for some of the assets on which the Consortium had placed no value, serve as evidence that the mining assets were undervalued. The Kafue Consortium reduced the valuation of the 'Aco' package by excluding some assets from the valuation.

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488 Interviews with Francis Kaunda, 20 October 2003; Valentine Chitalu, 22 October 2003 and John Lungu, 12 November 2003.
489 Interviews with Emmanuel Mutati, 18 November 2003 and Wilphred Katoto, 12 November 2003.
490 The replacement cost of the assets and the ore in the ground based on the then current value of finished copper.
491 Interview with Stuart Cruickshank, 28 October 2003.
492 Interview with Gilbert Temba, 13 October 2003.
493 Interview with Fred M'muembe, 14 October 2003.

The assets that were excluded were the Nchanga and Nkana package, the Chingola Refractory Ores (CROs),[494] Chibuluma South, for which no plan was provided, Nkana Synclinorium,[495] which was earmarked for later development[496] and the Nkana slag stockpiles,[497] despite the group having possessed the technology to treat the material at these mines. The resources on which the Kafue Consortium placed no value amounted to 429 million tons. Furthermore, the projected life of 10 years that the Kafue Consortium estimated for Nkana and the CROs was too conservative (Kaunda, 2002:62).

Additionally, the Nkana slag dumps, on which the Kafue Consortium put no value but wanted to include in the package that it envisaged to operate only in the 12th year was later sold to a former partner of the consortium, AVMIN, for US$50 million. AVMIN invested in modern smelting and leaching facilities at the plant almost from the outset. Moreover, the Chibuluma Mines that the Consortium wanted to include in the package for strategic reasons[498] were subsequently sold to Metorex for US$17.5 million. Also, the proposal of Metorex to immediately develop Chibuluma South, to phase in with the closure of Chibuluma West,[499] curtailed the excessive retrenchments of workers that would have accompanied the closure of Chibuluma West that the Kafue Consortium envisaged. A failure to develop Chibuluma South, with a lifespan of approximately 14 years, following the closure of Chibuluma West, would likely have turned the nearby Kalulushi town into a ghost town (Kaunda, 2002:62, 71, 72, 183).

Furthermore, by excluding from their calculations the considerable reductions in redundancy payments subsequent to the inclusion of houses sold to workers in their redundancy packages, the Kafue Consortium overstated in its valuation both the discounted rate at 20%[500] and the redundancy costs at US$30 million. Tax concessions

494 That involved minimal costs because it is a surface mine.
495 That contained about 221 million tons at 2.23% copper and 0.10% cobalt.
496 After 10 years.
497 That contained about 20 million tons at 1.10% copper and 0.72% cobalt and because these are on the surface, they are less costly to process.
498 With AVMIN claiming to have exploration licenses both north and south of Chibuluma South. The demand for the inclusion of Chibuluma Mines in package "A" was tantamount to land grabbing, according to Metorex (Kaunda, 2002:74).
499 That was then expected to run out in about 4 years.
500 Since the normal rate was between 10% and 15%.

that the Kafue Consortium sought were also more than those approved for the other mines. These entailed reductions of mineral royalty tax to 1%, withholding tax from 10% to 0% and of the import declaration fee from 5% to 0% (Kaunda, 2002:62, 63, 71, 72, 75, 76, 183).

Moreover, an alleged practice of Rothschild, the foreign advisors to the government, who assisted in valuing some of the packages,[501] of undervaluing the assets of the mines and divulging these values to the buyers,[502] possibly also increased the bargaining leverage of the Consortium over the Zambian government in the bidding process. The 'Kafue Consortium walkout' in London was in fact allegedly precipitated by the difference in the value that the foreign advisors divulged to the buyers and the higher value that Francis Kaunda proposed for the mines.[503] Evidence from the feasibility study of the buyers of the Chibuluma Mines that stocks worth about US$435 000 were excluded in the advisors' valuations of these mines[504] to some extent supports the claim that the advisors were inclined to underestimate the mining assets of Zambia.

However, TNCs would not always behave in the opportunistic fashion that marked the behaviour of the Kafue Consortium during the negotiating process. Furthermore, a discounted cash flow method of evaluating the value of assets, over an asset-based valuation, does not inherently favour the buyer. Rather, the poor economic position of the country that weakened the leverage of the government for demanding more for the mining assets and its poor capacity for also valuing the mines independently of the advisors and of the buyers and to assert higher prices for the mines, encouraged the mining TNCs to shift bids in their favour. The poor leverage of the government was therefore considerably to blame for its failure in obtaining a fair market value for the mines at the time.

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501 Interview with Valentine Chitalu, 22 October 2003.
502 Interview with Emmanuel Mutati, 18 November 2003.
503 Interview with Emmanuel Mutati, 18 November 2003.
504 Interview with Thomas Kabandama, 13 November 2003.

6.2.2 Advantages through concessions

Within a weak state, the mining TNCs, in particular Anglo American[505] and Mopani, were able to gain extensive additional concessions from the government for their operations at KCM and MCM respectively, in comparison to those granted to other mining TNCs that privatised earlier.[506] In turn, the government imposed very few obligations on the mining TNCs.[507] These additional concessions were also granted to the new buyers, viz. Vedanta Resources that took over majority ownership of KCM in 2004 and to J and W Holdings. J and W Holdings acquired both the Luanshya/Baluba mine, previously owned by Binani before it was placed under receivership, and Chambishi Metals that it took over from AVMIN.

The new buyers made the additional concessions conditional on concluding the sales of the mines.[508] Seemingly, the concessions were more the result of the poor bargaining leverage of the Zambian government, especially during the privatisation of the final assets of the ZCCM that made it vulnerable to the demands of these companies, rather than due to an independent government assessment of the merits of the concessions. The concessions continued during periods of high international prices (The Economist Intelligence Unit, 2007b:36).

The different concessions granted to the mining companies that were not extended to local businesses and the additional concessions granted to KCM and to MCM are elaborated upon in Table 6.1 (Fraser & Lungu, 2007:55, 62, 63, 65). To date, the companies continue to enjoy most of the concessions. The different types of concessions granted to the mining TNCs encompass concessions on company taxes, Value-Added Tax (VAT), royalties, customs duties and on other input tariffs. Certain concessions, more specific to some of the mining companies, were also granted to the various companies, especially to KCM (World Bank, 2002b:17; Regional Investor

505 Afforded largely through its knowledge of the dire economic position of the ZCCM and of foreign donor pressure imposed on the Zambian government to finalise the privatisation of the ZCCM, on account of its position as a board member and a minority owner of the ZCCM (interview with Silane Mwenechanya, 24 October 2003).

506 Interviews with Dave Phiri, 23 October 2003; Honourable Captain Moono, 2 December 2003; 24 November 2003; Silane Mwenechanya, 24 October 2003; Valentine Chitalu, 22 October 2003; Danny Kalyalya, 31 October 2003; Andrew Sardanis, 19 October 2003 and Fred M'muembe, 14 October 2003.

507 Interview with Andrew Sardanis, 19 October 2003.

508 Interview with Ohene Nyanin, 29 November 2003 and Honourable Captain Moono, 2 December 2003.

Survey, 2001:42).

The main company tax concessions applicable to all the mining TNCs entailed the pegging of mining company tax at 25%, compared to 35% for manufacturing companies (and alongside personal income tax or PAYE, of 37.5%, for many formal-sector workers).[509] Furthermore, the mining companies are allowed to deduct 100% of their fixed assets and capital expenditure from their accounting profit in the year in which it occurred, as tax allowance. The interest paid on loans and on taxes is also still tax-deductible for the mining TNCs.

Both the stability period and the carry-forward losses were applicable for 15 years and were broadened for KCM and MCM to 20 years, entitling them to subtract the losses made in year one of operations from the taxable profits in subsequent years (Fraser & Lungu, 2007:11, 15, 17). Moreover, KCM and MCM are still exempted from paying withholding tax on interest, dividends, royalties and management fees paid to shareholders and affiliates. The level of withholding tax for other mining companies is still 10%, except where double taxation agreements applied, in which case no withholding tax is payable (Kaunda, 2002:83; Transparency International, 2002:6).

Secondly, the mining companies are exempted from having to pay the 17.5% VAT, until the companies start making a profit. Thirdly, the mineral royalty tax of earlier privatised companies was reduced to 2% of gross turnover of the revenue of minerals produced in the mining sector, despite the Mines and Minerals Act suggesting a mineral royalty of 3% for companies that hold large-scale mining licences. KCM and MCM enjoyed an additional reduction in mineral royalty tax to only 0.6%. Mineral royalty tax was reduced even further to only 0.5% for a new investor, Equinox, that came on board after the ZCCM was privatised, for developing the undeveloped Lumwana mine (Fraser & Lungu, 2007:11, 15; Africa Confidential, 2006:4).

Fourthly, the concessions on customs and other duties that the mining companies enjoy

[509] More recently, though, personal income tax levels were reduced so as to provide relief to workers (The Economist Intelligence Unit, 2007b:29).

entail exemptions on import tax levied on machinery and equipment for five years if destined to be employed in the operations and in the exploration activities of the mining sector. The concessions on customs and other duties were also extended to other contracting firms that import machinery for the development of mining (Fraser & Lungu, 2007:11, 15, 17; The Economist Intelligence Unit, 2007b:9, 29). While other mining companies paid duties of up to 20% on consumables and spares, the aggregate rate of the concessions on import duties and tariffs of KCM and MCM was not to exceed 15% of the value of imported items for five years (Kaunda, 2002:83; Transparency International, 2002:6). Also, Equinox has been shielded for ten years from having to pay import duties on its operations at Lumwana (Kaunda, 2002:83; Africa Confidential, 2006:4).

Other tariff reductions entail a 5% reduction in the electricity levy of the earlier privatised mining TNCs to 10%. KCM and MCM are exempted from paying excise duties on the consumption of electricity and pay an additional reduced electricity tariff rate of 2.7 cents per kilowatt-hour for 15 years, instead of 3.3 cents per kilowatt-hour that applies to other mining companies. Until its departure from KCM, Anglo American also enjoyed significantly reduced tariffs on lime and oil inputs to the mines.

In addition to concessions on corporate taxes, VAT, royalties, duties and on electricity tariffs, the mining companies are also shielded from certain national laws. These include protection against several laws covering environmental pollution and from having to take over most of the liabilities of the ZCCM, such as pensions owed from the ZCCM to their employees (Fraser & Lungu, 2007:2; Africa Confidential, 2007:10). The mining companies are further allowed to externalise all their funds, proceeds, profits and dividends.

Furthermore, Anglo American demanded the retrenchment of many workers at the mines it was to take over and shifted the responsibility for the payment and the settlements of the redundancy packages of the laid-off employees onto the Zambian government. The government paid the redundancy packages through a US$65 million loan from the World Bank (Committee on Economic Affairs and Labour, 2001:70, 340; Africa Research Bulletin, 2000a:14302; Lungu, 2001:15). The state was also to bear the costs of the retrenchment packages of the employees that J and W retrenched before taking over RAMCOZ (the company intended to employ only 1 000 workers). Furthermore, J and W was allowed to close the Luanshya mine, since it planned to operate only the Baluba mine.[510]

Table 6.1: Concessions granted to privatised mining companies in Zambia

Concessions enjoyed by privatised mining companies	Additional concessions granted to KCM and MCM
Corporate tax concessions • A company tax of 25%, instead of 35% that is charged for non-mining companies and 30% for companies listed on the Lusaka Stock Exchange (LuSE) • The stability period is valid for 15 years • Carry-forward losses are valid for 15 years, as a tax concession. Non-mining companies are entitled to carry forward losses for only 10 years • Interests paid on loans are tax deductible • Tax allowance that includes 100% deductions of fixed assets and on capital expenditure from the accounting profit of mining companies that is not applicable to non-mining companies	**Corporate tax concessions** • Similar to that for earlier privatised mining companies, company tax was levelled at 25% • The stability period was increased to 20 years (compared to 15 years for the earlier privatised mines) • The carry-forward period for tax losses increased to 20 years • KCM and MCM were exempted from paying withholding tax on interests, dividends, royalties and management fees paid to shareholders and affiliates. For other companies, the existing level of withholding tax was 10%, except where double taxation agreements applied, in which case no withholding tax was payable
VAT • Full exemption on VAT of 17.5%. The suspension of VAT on imported mining equipment and that would be applicable until these companies make a profit. This also applies to new mining investors that had not, as yet, started production by mid-2008, namely, the Muliashi copper mine, owned by J and W Investments, and the Chambishi smelter, owned by China's NFCA	
Mineral royalty concessions • Royalty tax is reduced to 2%, which is often deferred	**Mineral royalty concessions** • Mineral royalty tax was reduced to 0.6% for KCM and MCM. Equinox enjoys a further reduction in mineral royalty tax to 0.5%

[510] Interview with Silane Mwenechanya, 24 October 2003.

Concessions enjoyed by privatised mining companies	**Additional concessions granted to KCM and MCM**
Duty concessions and other tariff reductions • Mining companies are exempted from customs or import duties on all imported capital items that are used for implementing the agreed programme of operations, in accordance with the Mines and Mineral Act • A 5% reduction on the electrification levy, or excise duty	**Duty concessions and other tariff reductions** • Duty rebates were extended to imported mining consumables, which were, however, capped at US$18 million per annum for 5 years[511] • The aggregate rate of import duty is not to exceed 15% of the value of the imported items. Other mining companies have to pay between 5% and 20% duty on most consumables and spares • Exemptions from paying excise duty on electricity consumed (Rural Electricity Levy), which was 10% for other mining companies in 2002 • The companies enjoy lower electricity tariffs of 2.7 cents per kilowatt-hour for 15 years, instead of 3.3 cents per kilowatt-hour that applied to other mining companies • Anglo American (through ZCI), obtained a 7-year contract for the supply of lime, at a fixed price of US$90 per ton, afforded from low costs of heavy fuel that Ndola Lime obtained from Indeni • The price for fuel was kept constant for KCM, despite the contract company, TST, wanting to increase the price of oil, and the high increases in the price of heavy fuel oil (HFO)[512] for other users • No council rates would be charged for KCM and MCM for 15 years
Other concessions • Companies were allowed to externalise 100% of their funds, proceeds, profit or dividends • CEC was allowed to keep its books in dollars, while paying taxes in kwachas • CEC enjoyed debt forgiveness and interests were cancelled to compensate it for reducing the electricity rate it charged KCM and MCM • Exemptions from certain environmental laws • Exemptions from taking over the liabilities of the ZCCM (eg. pensions due to employees from the ZCCM)	**Other concessions** • The social security contributions of KCM and MCM were paid to a South African-based social security company and not to NAPSA, a Zambian-based social security company • Anglo American was granted concessions to compensate for the lower internal rate of return it was able to obtain from the Nkana smelter it utilised, compared to the Mufulira Smelter that proved more efficient on account of its use of electricity • The costs and settlements of retrenchment packages of those employees that Anglo American did not want to employ, before KCM was privatised, were transferred to the Zambian government and paid through a US$65 million loan from the World Bank. Moreover, except for the 1 000 workers that

[511] One consignment of steel for the mines could, however, already go up to US$10 million, before any other consumables were imported (Kaunda, 2002:165).

[512] HFO, which accounts for about 55% of the cost of quicklime production, greatly increased during the negotiation period, rising by about 300% from April 1998, when it was US$0.17 per kilogram, to US$0.51 per kilogram in late 1999/early 2000.

Concessions enjoyed by privatised mining companies	**Additional concessions granted to KCM and MCM**
	J and W wanted to retain at the Luanshya Mines by 2004, the government would possibly pay off all the workers that J and W intended to lay off • KCM and MCM are indemnified, for 20 years, from on-going environmental liabilities, while in compliance with their environmental plans • ZCI received a five-year option to buy the Nkana smelter • ZCI got the legislation changed to include its incentives as a statutory instrument

Sources: Africa Research Bulletin (2000a:14302); Committee on Economic Affairs and Labour (2001:48, 70, 340); Dow Jones Commodities News via Comtex (12 June 2008); Kaunda (2002:83, 131, 148, 165); Lungu (2001:15); Fraser & Lungu (2007:2); Transparency International (2002:6, 2007:2), Africa Confidential (2007:10); and interviews with Danny Kalyalya, 31 October 2003; John Lungu, 12 November 2003; Zion Simwanza, 1 December 2003; Stuart Cruickshank, 28 October 2003; Honourable Dipak Patel, 15 October 2003; Stella Motale, 23 October 2003; Thomas Kabandama, 13 November 2003; Andrew Hickman, 7 November 2003; Liang Tun, 4 November 2003; Andrew Sardanis, 19 October 2003; Andygean Luombe, 8 October 2003; Gary Loop, 29 October 2003; L. M. Lishomwa, 29 October 2003 and Silane Mwenechanya, 24 October 2003.

Most significantly, Anglo American ensured a change in the Zambian legislation allowing for the inclusion into the constitution the provisions of its development agreement that provided for the incentives. The change made government compliance to the concessions granted to the company legally enforceable and subject to an international arbitration process.[513] Subsequently, other mining companies followed suit, through renegotiations with the government, to make their incentives legally enforceable as well.

It is noted from the above discussion that within a weak state, the TNCs tended to use their dominant bargaining power to shift benefits in their favour. The dominant bargaining leverage of the mining TNCs encouraged them to consolidate their advantages in the mining industry by collaboration, through the formation of a consortium, in the bidding process for the privatisation of the mines. It also enabled them to extract highly favourable concessions from the government.

The negative outcomes arising from the dominant bargaining leverage of mining TNCs

[513] Interviews with Honourable Dipak Patel, 15 October 2003 and Silane Mwenechanya, 24 October 2003.

in Zambia contradict the relative optimism of the proponents of bargaining as to the long-term negotiating prospects that developing countries possess for extracting favourable terms from TNCs. Rather, these outcomes support the structuralists' argument that gains from foreign interests through bargaining are not inevitable (Padayachee, 1995:164). The bargaining proponents further failed to take into account the impact of other factors and interest group divergences in influencing the decisions of the Zambian government.

In particular, pressure from donors that the mines be privatised swiftly and the higher bargaining edge that mining TNCs possessed enabling them to make increasing demands on the Zambian government, greatly reduced the leverage of the MMD government to extract favourable gains from mining TNCs for the Zambian economy. The significant demands that mining TNCs were able to exert on the weak MMD government that often lowered benefits for the host country, further validates the argument that mining activities require strong government bargaining skills, to ensure that the greatest possible share of the rent element from mining accrues to the host country (Chang, 1998:238).

6.3 RETURNS TO THE ZAMBIAN ECONOMY FROM THE EXTRACTION OF COPPER

Main determinants of returns for the national economy from mining investigated below are: (i) government tax revenue from mining; (ii) the repatriation of mining resources; (iii) Zambia's foreign currency earnings from mining; and (iv) the roles of TNCs in promoting the development of local capital, in particular the development of local suppliers and workers in the mining sector.

It is noted in Chapter 3 that adequate capturing of rent of exhaustible resources by the government is fundamental for promoting national development and to maximise long-term revenue to compensate for their limited income and employment potential. In particular, sufficient tax revenue is necessary to increase rent capturing, in addition to reinvestment of the capital allowance component from mining in alternative forms of capital assets viz. investment in new wealth and forms of *renewable* capital, such as human, social and physical capital to achieve sustainable development, beyond mining (see, for example, Pedro, 2004:6; Blignaut & Hassan, 2002:99-101; Blignaut & Hassan, cited in Cawood *et al*., 2001:157). Excessive repatriation of profits would reduce or cancel out gains through investment and tax revenue and may even amount to a draining of the surpluses of developing countries. An investigation of the generation of effective renewable capital in Zambia from mining surpluses is pursued by assessing the benefits from mining to the local suppliers and workers in Zambia.

6.3.1 Government tax revenue from mining

Adequate fiscal take from mining,[514] balancing the firms' willingness to invest and the maximisation of rent capturing for the government from mining, is crucial to enable the government to meet the requirements of capital generation for reinvestment in projects and social capital (see, for example, Lewis, 1982; Auty, 1993, cited in Cawood *et al*., 2001:220, 221). Too low taxes would result in rent from copper extraction accruing mostly to mining TNCs (Macfarlane, cited in Cawood *et al*., 2001:220, 221). While low taxes from the extraction of copper would serve profit-maximising aims of mining TNCs these would diminish the share of surpluses obtainable from mining to the Zambian economy and people.

The discussion below investigates the fiscal take of the government from mining TNCs in Zambia by reviewing firstly the government taxes from mining and the impact of the concessions granted to mining TNCs on government revenue. Next, the motivation for higher mining taxes from TNCs is considered. The leverage of the government in increasing government revenue from mining TNCs is then explored.

6.3.1.1 <u>Government taxes and the impact of concessions on government revenue</u>

Unlike the case under government ownership, income to the government from mining under private TNCs' ownership is not obtained directly from sales and profits from the mines but is confined under private ownership of the mines to various taxes levied on

[514] Considered by various theorists as the strongest linkage between the mining sector and the national economy.

the mining TNCs. The mining taxes include income tax of employees, border tax paid on imports and exports, corporate tax on profits and mineral royalties on the sales of copper. Further revenue is obtained from 15% withholding tax and from reverse VAT (whereby mining companies have to pay tax when they outsource work to foreign workers, while local expertise is available).[515]

The extensive tax concessions granted to mining TNCs, especially on corporate tax, VAT, duty tax, mineral royalty tax and the additional concessions granted to the latter privatised mines, KCM and MCM (detailed in Table 6.1), reduced even further the potential government tax revenue obtainable from private mining TNCs. The tax revenue from mining is illustrated in Figures 4.22 and 4.23 of Chapter 4 (Fraser & Lungu, 2007:55). In the first year of the privatisation of some of the mines in 1997, tax and other concessions granted to the mining TNCs cost the government ZK18 billion (US$7.83 million) in lost revenue. The additional concessions extended to KCM and to MCM in 2000 exacerbated the losses in government revenue (Afronet *et al*., 2001:16, 42).

In the short term, under private ownership of all the major copper mines, mining tax (namely total company tax, withholding tax and mineral royalty tax but excluding PAYE for workers), remained at very low levels of less than US$2.4 million between 2000 and 2004. This was largely as a result of the various concessions that mining TNCs continue to enjoy. However, during the copper price boom mining tax rose from a mere US$1.3 million in 2004 to US$10.1 million in 2005 and to US$49.7 million in 2006. It increased further to about US$174.3 million in 2007 (Figure 4.22). These increases in government revenue from mining from 2005-06 were a considerable improvement on the low levels of 1998 and 1999, before the transfer of ownership of all the major copper mines to private ownership and from even more marginal levels until 2004, under private ownership.

However, the higher levels attained during the copper price boom were still

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515 Interview with Thomas Kabandama, 13 November 2003.

significantly lower than the contribution that the ZCCM made to the national treasury in 1991, under government ownership (Fraser & Lungu, 2007:55). Figure 4.22 shows that the 1990-91 financial year, mining taxes were about US$236.7 million and in 1991-92 these were US$194.6 million. However, mining taxes fell to about US$42 million in the 1994-95 financial year and continued to decline to US$13.1 million in 1996.

The poor contribution of taxes from mining to total government revenue is further mirrored in the fact that at the height of the copper price boom the share of mining taxes rose to only about 10% in 2006. In Chile the contribution was 20% (Bova, 2009:18-19). The low Marginal Effective Tax Rate (METR – describing how much each industrial sector is taxed) of the mining sector, at around 0%,[516] further manifests the poor contribution of the mining sector to government revenue (Fraser & Lungu, 2007:55).

Another surprising aspect of the Zambian taxation system is the fact that PAYE taxes from mining employees' salaries[517] constitute the government's main source of revenue from the mining sector (Figure 4.24). As such, personal income tax generated an unusually high share of the total tax take, of just under one third of the total government revenue, in 2003. In contrast, by 2006 during the copper price boom, the gains in government revenue from mining corporate tax to US$36.34 million (that was negligible until 2005) still contributed very little to government revenue, even less than smaller sectors, such as the financial services and telecoms sectors (Fraser & Lungu, 2007:55, 56, 61, 62). Corporate tax increased further to US$156.73 million in 2007. Section 4.4.20 explains the trends in government tax obtained from mining.

The overall company tax[518] contributed only 2.5% of total government revenue in 2006, while it had generally brought in over 6% of the total annual income of the government in the 1990s (Fraser & Lungu, 2007:62). Likely transfer pricing practices aided by the possibility to remit 100% of their mining profit out of Zambia[519] probably accounted,

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516 According to the calculations of the World Bank.

517 Interviews with Danny Kalyalya, 31 October 2003; Reibner Hoffner, 15 October 2003 and Thomas Kabandama, 13 November 2003.

518 From mining and non-mining companies.

519 Interview with David Chilipamushi, 20 October 2003.

together with the concessions, for the poor corporate tax gains and other taxes for the government from mining. In particular, concessions allowing mining companies to carry losses from previous years forward for 15 years (and for 20 years in the case of KCM and MCM) and to write them off against future profits and to deduct 100% of their capital expenditure and fixed assets from the accounting profit as tax allowance greatly reduced the corporate tax base for the Zambian government.[520] The enormity of the losses is well illustrated in the significant differences in accounting losses in the first year of the operations of the Chibuluma mines that amounted to US$1.8 million, and net losses that came to US$18.8 million, after US$17 million worth of assets bought from the government (100% of fixed assets) was taken into account for that particular year.[521]

Other non-corporate tax concessions granted to mining TNCs also significantly reduced the potential government revenue obtainable from taxing mining companies. These include the lowering of royalty tax for extraction[522] that led to mining TNCs contributing to just 0.2% of government revenue in 2003,[523] VAT on goods bought locally and duty exemptions on various imports. In particular, duty exemptions significantly lowered the potential government revenue, especially in light of the METR on machinery of the mining sector enjoying the largest subsidy (-18.3 percent) received in any sector and asset (Fraser & Lungu, 2007:62). Moreover, the strategy of mining TNCs of building the labour costs into the capital equipment expenditure, making the isolation of the labour content difficult, enables mining TNCs to pay no or very low reverse VAT (Fraser & Lungu, 2007:55, 56, 62).[524] Furthermore, reductions on other tariffs, such as the concessions on excise duties granted to some of the mining companies, likely contributed to the collection of excise duties being 10.9% below target in 2003 (Ministry of Finance and National Planning, 2003:5).

Furthermore, the advantage often cited by mining TNCs that price participation clauses,

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520 Interviews with Thomas Kabandama, 13 November 2003 and Ladslous Mwansa, 7 October 2003.
521 Interview with Thomas Kabandama, 13 November 2003.
522 Namely a tax on the revenue from the sales of copper.
523 Also, since 2003, the Zambian government no longer gains royalties from Bwana Mkubwa (which paid mineral royalty tax on Zambian copper for 5 years), as the company now obtains its copper ore from the DRC, while processing it in Zambia (interview with Andrew Hickman, 7 November 2003).
524 Interview with Thomas Kabandama, 13 November 2003.

whereby the government is able to claim back a percentage of each sale made if the price of copper at the LME exceeds a specific benchmark (US$2 700 per ton), would increase government revenue is misleading. This is because the tax-deductible incentives granted to mining companies for the price participation payments would cancel out gains in government revenue from price participation. Also, the capping of price participation benefits to the government, at US$9 million per annum for MCM further reduces this benefit (Fraser & Lungu, 2007:15, 57, 64, 65; ZPA, 2000c:33). In addition, returns in government revenue by way of its minority interests in the mining companies, through tax dividends paid to the ZCCM-IH, would only emerge once the companies commence reaping major profits (Fraser & Lungu, 2007:57). Despite the boom, the government did not receive any dividends from mining TNCs by 2008, through its stake in the privatised mining companies[525] (varying from 10% to 21%), mainly owing to the accumulation of liabilities (Ministry of Finance and National Planning, cited in Bova, 2009:11).

Owing to the long-term nature of the concessions, higher gains for the government from tax revenue will be achieved not when mining companies begin to make a profit but only once they become eligible for tax, in some cases after 20 years. In the process the government will forfeit substantial potential revenue from mining.[526] These concessions would, at times, outlive the life cycle of some of the mines (Committee on Economic Affairs and Labour, 2000:42-43; Fraser & Lungu, 2007:2; The Economist Intelligence Unit, 2007b:36).

Moreover, despite the general increase in government revenue in recent years, government revenue as a percentage of GDP has in fact dropped sharply since 2001, even during the years of the copper boom, and became volatile (Figure 4.22 of Chapter 4). This indicates that the government's share of benefits during the boom was in fact declining (Bova, 2009:20). Accordingly, the government taxes from mining would in the absence of interventions to reduce the concessions, likely remain low for a

[525] Interview with Silane Mwenechanya, 24 October 2003.
[526] Interviews with Danny Kalyalya, 31 October 2003; Honourable Captain Moono, 2 December 2003; Bernadette Mwakacheya, 17 October 2003; Fred M'muembe, 14 October 2003; Silane Mwenechanya, 24 October 2003 and Charles Muchimba, 18 November 2003.

considerable time,[527] precluding greater benefits for Zambia from better performance of the mining sector following increased investments in the mines under the ownership of TNCs (The Economist Intelligence Unit, 2007b:29, 36).

6.3.1.2 Motivation for higher mining taxes

The increases in PAYE and VAT to boost government revenue during Chiluba's government to make up for the shortfall in revenue obtainable from the mining sector, were highly unsuitable for Zambia. This is because the unusually higher tax on workers through PAYE of 37.5%, which had been significantly raised since 1991, and of VAT of 17.5% (from which TNCs are excluded), especially on agricultural produce, which pushed up food prices, increased the tax burden of the poorer sectors of society (Fraser & Lungu, 2007:61; Africa Confidential, 2006:4). Moreover, increases in non-tax revenues, such as user fees or utilities bills for health and educational services, also lowered public access to these services (The Economist Intelligence Unit, 2007b:17, 18-19).[528]

Concessions represent a highly inappropriate policy for non-renewable resources that instead require the maximising of rent to compensate for their finite opportunities and to enable the reinvestment of the revenue from mining into renewable resources to ensure more sustainable development. Rather, higher import tariff rates, corporate tax and mineral royalty rates,[529] which would be less disadvantageous to the poor, would be more appropriate and would considerably improve government revenue from mining (Fraser & Lungu, 2007:61, 62, 64, 65). Higher copper prices, the poor corporate behaviour of some mining companies and the unlikelihood that most of the mining companies would have volunteered to pay more in taxes further justify an alteration of the concessions that mining companies enjoy. However, mainly as a result of the

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527 Interviews with Emmanuel Mutati, 18 November 2003; Thomas Kabandama, 13 November 2003; Andrew Hickman, 7 November 2003 and John Lungu, 12 November 2003.

528 However, the reintroduction in 2002 of a free basic education policy led to an upturn in primary-school enrolment. and the raising of the numbers of medical personnel and the scrapping of user fees in rural clinics in April 2006, facilitated through debt relief granted to the country, in 2005-2006, would improve access to health facilities in Zambia (The Economist Intelligence Unit, 2007b:18-19).

529 Possibly to an average of 2.5% that the IMF recommended in its 2005 report, on the overall Zambian tax policy, prepared for the government. A 2.5% mineral royalty represents a significantly less radical approach than what the Chilean government adopted in its 'pro-poor' mining policy and is still at the lower end of international averages and compared to their neighbours. An IMF survey of tax and royalty rates in developing country found that no other African country is charging royalty rates below two per cent (Fraser & Lungu, 2007:62).

dramatic increases in the price of copper since 2004, First Quantum, still well within the period of its tax holiday, decided to start paying company taxes that contributed US$19 million towards the revenue of the Zambia Revenue Authority in 2006 (Fraser & Lungu, 2007:57).[530]

6.3.1.3 Government leverage to increase tax revenue from mining TNCs

Public and donor pressures forced the Mwanawasa government to pass a new tax regime, via the Income Tax Amendment Bill introduced in April 2008, that prescribes increases in several taxes from mining and the removal of some mining incentives (Action Aid International *et al*., 2009:26, 47; The Economist Intelligence Unit, 2008a:10, 11, 2008b:17).[531] Key features of the tax amendments were the imposition of an additional 25% windfall tax and a variable profit tax on mining exports. The windfall tax was to apply when the international copper price rose above US$5 512 a ton. The variable profit tax (ranging from 0% to 15%) became payable if the taxable income of companies was above 8%. The windfall tax[532] would have enabled the government to collect part of the extra rent generated from mining during times of windfall profit. The amended tax laws further allowed the companies to deduct only 25% of capital expenditure in each year of mining production (instead of 100%); increase royalties to 3%, rather than 0.6%; and raise corporate tax to 30% from 25% (Action Aid International *et al*., 2009:26, 27, 32, 47; Bank of Zambia,[533] 2010; Zulu, 2008).

High copper prices and increased sunk costs that mining companies incurred especially during the copper price boom that raised the costs to mining companies of pulling out of Zambia are likely to deter withdrawals and raise the leverage of the government to make demands on the mining companies. However, certain constraints continue to prevent the government from significantly reducing concessions, introducing additional tax over those stated in the Income Tax Amendment Bill of 2008 and from re-imposing levies or increases in import duty tariff rates in the mining sector. The constraints entail

[530] The decision was possibly to allay protests against the lack of redistribution of the high gains that the private mining companies enjoy.
[531] The incentives were introduced at a time when copper prices were low and were deemed necessary to attract investors.
[532] That was already withdrawn in 2009.
[533] Current state of affairs confirmed by e-mail on 17 May 2010 from: Dinde Simacheche, SDINDE@boz.zm, Bank of Zambia, in response to questions by author.

hostility of the mining companies to the new tax regime,[534] capacity constraints of the government and the possibility that those mining companies that had their concessions inserted in the Zambian constitution (Statutory Instrument 32)[535] are legally able to dispute such increases through international arbitration. The gazetting of the concessions of several mining TNCs in the legislation[536] securely locks the government into demands made by the TNCs, making it extremely difficult to reduce these concessions (The Economist Intelligence Unit, 2007b:36; Fraser & Lungu, 2007:15).[537] World Trade Organisation (WTO) restrictions and various free trade agreements to which Zambia is a signatory also limit reductions in trade concessions (Fraser & Lungu, 2007:61, 62, 64; The Economist Intelligence Unit, 2008a:4, 10; Africa Confidential, 2007:10).

As a result, the increases of some of the taxes through the Income Tax Amendment Bill were short-lived. Pressure from mining companies to take the matter to international arbitration and the fall in the copper prices in 2009 from the high levels of June 2008 obliged the government to reduce or abolish some of the new tax increases. This was ruled in the 2009 National Budget (Action Aid International, *et al*., 2009:58; Bank of Zambia,[538] 2010). Accordingly, following the announcement in the National Budget the windfall tax was withdrawn and the capital allowance of 100% was reinstated.

Moreover, the provision to treat income and losses from hedging activities as a separate activity from mining was repealed. Furthermore, the National Budget made provisions for the removal of customs duties of certain imports.[539] The difficulty the government

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534 Already, some investors blame the freezing of new mining projects on uncertainties in the mining industry, the higher tax regime introduced in the mining sector, in 2008 and because of difficulties in raising funds for mining projects (The Economist Intelligence Unit, 2008a:2, 11). In 2008 MCM, the country's second-largest producer, shelved plans to sink a new shaft that could have created employment for 2000 people and increased output at the Mufulira mine, because of difficulties it experienced in raising capital (Chekwe-Puta, cited in The Economist Intelligence Unit, 2008a:11).

535 Interviews with L. M. Lishomwa, 29 October 2003; M. Shandavu, 10 October 2003 and Honourable Dipak Patel, 15 October 2003.

536 Bwana Mkubwa also intended to have their development agreement gazetted in the Zambian legislation (interviews with Andrew Hickman, 7 November 2003; Honourable Captain Moono, 2 December 2003 and Zion Simwanza, 1 December 2003).

537 By increasing corporate tax, from 25% to 30%, raising royalty taxes to 2.5%, and by reintroducing withholding tax on dividends, interests, royalties, management fees and the payments to affiliates or subcontractors in the mining sector, at a standard rate of 15%.

538 Confirmed by e-mail on 17 May 2010 from: Dinde Simacheche, SDINDE@boz.zm, Bank of Zambia, in response to questions by author.

539 For instance, copper flakes, powder and blisters were exempted from custom duties; excise duty on heavy fuel oils were reduced from 30% to 15%; and the import VAT deferment scheme were extended to include copper and cobalt concentrates (Bank

experienced in unilaterally reducing the concessions granted to mining TNCs indicates that lengthy re-negotiations between the government and the mining companies would be necessary to enable greater benefits for Zambia from copper mining (Fraser & Lungu, 2007:62, 65; The Economist Intelligence Unit, 2007b:36).

The poor gains in government taxes under private TNCs' ownership of the mines discount the neo-classical argument that privatisation plays an important role in increasing government revenue, in addition to revenue from the proceeds from the sales of the mines. Rather, the limited tax income from privatisation, among other factors, reduces a successful outcome of the privatisation process, as is argued by Cook and Kirkpatrick (2000a:121). However, rather than due to an inherent flaw of the operations of TNCs in host countries, the weak returns in government revenue under TNCs' ownership of the mines seem largely the outcome of the poor bargaining leverage of the host government, enabling the mining TNCs to extract excessive concessions from the government.

The excessive concessions that mining TNCs were able to extract from the Zambian government again challenge the bargaining proponents' relative optimism regarding the negotiating prospects that developing host countries possess to extract beneficial terms from the activities of TNCs. Conversely, the poor gains that the weak government obtained from the mining TNCs, through taxes, reinforce the argument of developmental state theorists that a strong capacity of the government is fundamental in ensuring more economic benefits for countries from the activities of TNCs.

6.3.2 Repatriation of mining resources

High repatriation of profits under private TNCs' ownership of the mines, also through possible transfer pricing policies, reduced rent for the Zambian government from the extraction of copper under TNCs' ownership of the mines. This represented a large drain on Zambia's exhaustible resource. The difficulties of getting figures on transfer pricing practices and on the exact amount of mining revenue repatriated out of Zambia

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of Zambia (confirmed by e-mail on 17 May 2010 from: Dinde Simacheche, SDINDE@boz.zm, Bank of Zambia, in response to questions by author).

since the mines were privatised, make it impossible to determine precisely the extent of these practices of TNCs in more recent years. The income balance account, illustrated in Figure 4.10 of Chapter 4, does though provide an indication of the repatriation of profits of mining TNCs.

It is noted from the income balance account that at the time of the unprecedented boom in the price of copper during 2005-2006, a high repatriation of profit took place. This is depicted in the dramatic fall in the income balance of Zambia from -US$410 million in 2004, to -US$609 million in 2005, and finally to -US$1 005 million in 2006, at the time that the country enjoyed significant increases in its GDP from 2005 and 2006. The decline indicates that a large portion of gains from mining surpluses during the boom was lost to the Zambian economy. Weaknesses in certain regulatory and policy measures of the government, however, continue to facilitate the repatriation of profits from mining.

6.3.3 Foreign currency earnings for Zambia from mining

Mining TNCs have significant leverage in influencing Zambia's foreign currency earnings, on account of the foreign earnings from copper sales (Zambia's dominant export earner) accruing to them under their ownership of the mines. Under state ownership of the mines these accrued to the Zambian government. The externalisation of profits to offshore accounts, also through transfer pricing practices, greatly contributed to the high volatility (Figure 4.13 of Chapter 4) and lower foreign currency earnings accruing to Zambia from mining than was expected under TNCs' ownership of the mines.[540] The failure of TNCs to fulfil all their investment obligations and the high concessions mining TNCs enjoy, further reduced foreign currency earnings for the country from mining. The foreign currency reserve levels are discussed in Section 4.4.12 of Chapter 4.

Excessive outflows of mining surpluses undermined the stability of Zambia's foreign exchange reserves with likely disastrous outcomes for the country, especially in the

[540] Interview with John Kangwa, 21 November 2003.

context of the country's limited foreign exchange reserves. The repatriation of mining surpluses increased at the height of the copper price boom (Figure 4.4.9 of Chapter 4). Accordingly, the increases in foreign exchange reserves, especially in 2005 and 2006, were most likely attributable to the highly significant debt forgiveness that was extended to Zambia, rather than to TNCs' ownership of the mines.

The repatriation of a significant portion of foreign currency earnings under private ownership of the mines further diminished the country's savings from mining. Savings from mining would enable the establishment of a stabilisation fund, necessary to reduce the negative impact of high volatility in the foreign currency reserves, owing to fluctuations in the price of copper. Furthermore, the far more aggressive auction system, whereby private mining companies tend to deal only with the banks that offer the keenest rates, encouraged bidding wars among the banks, benefiting the mining TNCs, at the expense of the banks in Zambia (Africa Research Bulletin, 2001c:14687). Additionally, a shortage of foreign exchange in a strongly import-dependent economy greatly increased the costs of imported inputs for the local supply industries to the mining sector (cost-push inflation), reducing local entrepreneurial capacities that are highly dependent on imports for manufacturing inputs.

The influence that mining TNCs possess on the level of foreign currency earnings also impact on the exchange rate, illustrated in Figure 4.12 of Chapter 4. The repatriation of mining profit and strategies of TNCs to manipulate the exchange rate (such as by way of withholding foreign exchange obtained from the sales of copper from the BoZ)[541] were greatly responsible for the high volatility and for the significant devaluation of the kwacha to the US dollar and the rand under private ownership of the mines before 2004.[542] It is noted in Section 4.4.11 of Chapter 4 that the value of the kwacha dropped from about US$1=ZK42 in 1990 to about US$1=ZK1 282 in 1996, immediately before the commencement of the privatisation of the mines in 1999, to US$1=ZK2 632, before the last and most lucrative mines were privatised. The value plunged further to

[541] That they for example employed as bargaining chips against the government to hedge themselves against increases in workers' salaries during negotiations on the salaries of workers (Africa Research Bulletin, 2001c:14687; Van Buren, 2003:1151).
[542] Ex-President Chiluba blamed the siphoning off of foreign exchange out of Zambia by new mine owners and other foreign investors for the fall in the value of the kwacha under TNCs' ownership of the mines (Africa Research Bulletin, 2001c:14687).

US$1=ZK4 157 in 2000 and US$1=ZK4 771 in 2004, under private ownership of the mines.

An unstable exchange rate limits, among other things, export diversification (World Bank, 2002a:18; Nalwamba, 2002:25).[543] In contrast, the continued leverage that TNCs have in influencing the levels of foreign currency reserves and the exchange rate of the kwacha in Zambia[544] enable them to extract more favourable outcomes in negotiations with the government.[545] The tendency of mining TNCs to function in foreign currencies, mainly in US dollars, protects them somewhat against the depreciation of the kwacha to the dollar and is in fact highly beneficial to the foreign mining companies that receive payments for their copper and cobalt exports in hard currencies. Weaknesses in government policies, elaborated upon in Section 6.5.1.8, also greatly facilitate the externalisation of foreign exchange from mining.

6.3.4 The roles of TNCs in promoting the development of local capital

This section examines the benefits from mining to local capital, namely the local suppliers and workers in Zambia, under the ownership of TNCs that are necessary for more sustainable development from the exploitation of mining resources. The development of local capital would be gauged in particular by way of the advancement of local backward-linked suppliers to the mines, higher employment and the human capital development of Zambians.

6.3.4.1 Local suppliers

With the exception of Binani, increased investment and the greater resources of mining TNCs for payments to suppliers[546] encouraged the development of more supply companies to the mining sector in the Copperbelt[547] from what was the case immediately prior to the privatisation of the mines, that generated higher employment levels. Delays in payments from the ZCCM and especially the inability of various local industries to

543 Interview with Silane Mwenechanya, 24 October 2003.
544 By withholding dollars to effect a depreciation of the kwacha and by changing dollars into kwachas if an appreciation of the kwacha becomes desirable for TNCs.
545 Interview with John Lungu, 12 November 2003.
546 Interview with Willie Sweta, 15 December 2001.
547 Interview with Willie Sweta, 15 December 2001.

compete in a liberalised environment were largely responsible for the closing down of many mining companies before the mines were privatised (discussed in Section 4.2.2.1 of Chapter 4). The repayment of government debts, worth about K227 billion,[548] to the suppliers of the ZCCM from an EU grant, however, also facilitated the process.

The strong influence of the mines for developing backward linkages is depicted in the high coefficient of 2.4 that the mining sector possessed for backward linkages in 2001 according to the IQ model. This indicates that for each kwacha of copper output produced, 2.4 kwacha from other sectors' inputs were generated (World Bank, 2002a:14).[549] In contrast, the coefficient for the forward linkage of the mining sector, of about 1.5[550] in 2001, is weak, since the mining sector does not directly provide inputs to other sectors and because almost all of the output are for exports (World Bank, 2002a:14).[551]

However, a closer examination of the benefits to local suppliers under TNCs' ownership reveals that the growth was predominantly in the service sector that is less labour intensive, rather than in the manufacturing sector, limiting greater employment benefits for Zambia from the high coefficient for backward linkages in the mining sector. The contribution of the service sector to GDP increased considerably in 1994 to 43.8% from 30.2% in 1993, consequent to the introduction of stricter SAPs. The service sector continued to grow under private ownership of the mines to 57.5% in 2007, moving the sector from fourth position in 1992 to first position in 2007 (Figure 4.6). This shifted the economy towards a service-driven economy (elaborated upon in Section 4.4.4 of Chapter 4) (The Economist Intelligence Unit, 2002:28, 2008b:20; Mwanawina & Mulungushi, 2002:30).

The potential benefits that a strong coefficient for backward linkages hold for local suppliers are further eclipsed by the regular practice of mining TNCs to replace local

[548] Interview with Danny Kalyalya, 15 December 2001.
[549] The IQ coefficient is 1.1 for agriculture, 2.1 for manufacturing and 1.9 for finance.
[550] Compared to 1.8 in agriculture, 2.4 for manufacturing and 3.8 in finance.
[551] Accordingly, Zambia imports a wide range of manufacturing goods produced from copper (World Bank, 2002a:14; Seidman, 1977:222).

companies in the procurement of mining inputs with likely cheaper and better quality imports from foreign manufacturers and suppliers. In particular, South Africa consolidated its position as the pre-eminent source of Zambia's imports, supplying a wide range of goods and services to Zambia. These include mining equipment and also non-capital goods,[552] such as food, security, cleaning and building materials (The Economist Intelligence Unit, 2007b:16, 42).

The mining TNCs even tended to buy copper cables from outside Zambia, rather than from Metal Fabricators of Zambia Limited (ZAMEFA),[553] the only copper cable-producing company in Zambia that used to supply the ZCCM with copper cable inputs.[554] The mining companies also increasingly import refined petroleum products, rather than sourcing these from the Indeni refinery in Zambia, partly owing to repeated domestic supply disruptions, making petroleum a major component of the import bill. Many maintenance and repair services, largely because of guarantees that are in place, will also typically come from the same foreign source, at least for the first five years (Fraser & Lungu, 2007:59; The Economist Intelligence Unit, 2007b:41).

Moreover, while Zambians are able to tender for smaller purchases,[555] perhaps reflecting a lack of capacity in Zambian businesses to supply high-cost goods, foreign companies are given sole suppliership for more expensive inputs into the mines. The high amount of inputs that are imported under private ownership of the mines is depicted in the dramatic and progressive increases in merchandised imports into Zambia from 2000 to 2007, mainly as a result of the substantial import component that greater investment in the mining sector holds (refer to Figure 4.9 of Chapter 4). Imports rose by 28% from 2000 to 2001, when they reached US$1 253 million, primarily owing to sharp increases in petroleum oil prices, a major component of the import bill, with capital goods accounting for the remainder.

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552 Despite the capability of several industries and suppliers in Zambia to supply some of these inputs to the mines (Fraser & Lungu, 2007:4, 58, 60).

553 That added value to copper through the manufacturing of copper cables, achieved under the Kaunda government's protectionist policies.

554 Interview with Alick Lungu, 20 December 2001.

555 Interview with Eddy Kapungulya, 13 November 2003.

Imports increased further to US$1 393 million in 2003. Subsequently, they almost doubled in 2006 to US$2 634 million, from the 2003 level, and rose even further to US$3 622 million in 2007 (The Economist Intelligence Unit, 2008b:23). However, imports in more recent years were more than offset by rising copper exports, due to the increases in the copper price from 2004 to 2006, leading to a fall in the drag that net trade placed on GDP (The Economist Intelligence Unit, 2007b:26).

Allegedly, in some instances the mining companies do not necessarily select suppliers on the basis of *x*-efficiency objectives but to favour their subsidiary supplier companies. Such alleged practices increase the opportunity of mining TNCs to earn monopoly profits, restrict competition, facilitate transfer-pricing practices[556] and limit multiplier benefits for local suppliers from the privatisation of the mines (Fraser & Lungu, 2007:59). In particular, Anglo American is alleged to have imported a number of its inputs into the KCM from its subsidiaries in South Africa.[557] Some Zambian suppliers allege that Mopani also tends to support South African suppliers.[558] Furthermore, NFCA favours equipment and service inputs from its Head Office, Transmetal Industrial Corporation of China, a Chinese SOE,[559] according to its own managers.

Additionally, the benefits of increased Zambian participation are possibly, at times, reduced because some South African supply companies allegedly disguise their effective foreign ownership in Zambia by using Zambians merely as fronts.[560] However, the high volume of supplies, the many cross-holdings and side-holdings that several mining companies possess and the controlling of their stakes through offshore companies make detection of collusion in the purchase of supplies difficult through a normal auditing process.[561] Furthermore, difficulties in obtaining data from mining TNCs on their suppliers has made it impossible within the scope of the study to independently confirm and to gauge the extent of TNCs' practices to substitute Zambian suppliers.

556 Interview with Honourable Eugene Appel, 24 November 2003.
557 Interviews with Honourable Eugene Appel, 24 November 2003 and L. M. Lishomwa, 29 October 2003.
558 Interview with James Chalwe, 23 November 2003.
559 Interviews with Liang Tun, 4 November 2003 and Yu Zhongqin, 4 November 2003.
560 Interview with Alick Lungu, 20 December 2001.
561 Interview with Simon Capper, 30 October 2003.

Nonetheless, an investigation of several indicators delineating manufacturing performance provides some indication of the benefits of mining to local backward linkages to the mining companies. Figure 4.3 of Chapter 4 shows that the average manufacturing growth rate increased under the TNCs' ownership of the mines. However, the increases took place from the very low base of 1998.

Moreover, it is noted in Section 4.4.3 of Chapter 4 that the growth was largely confined to the production of non-capital consumer goods mainly in the food, beverage and tobacco production, rather than in the local backward-linked industries to the mining sector. These commodities contributed about 65.8% to total manufacturing output in 2007, from 59.3% in 2000 (The Economist Intelligence Unit, 2008b:19; Central Statistical Office, 2008). The increasing growth primarily in consumer commodities reduces diversity in the manufacturing sector.

Furthermore, in spite of the better performance of the mining sector from 2004 to 2006, Figures 4.4 and 4.5 of Chapter 4 show that the contribution of manufacturing to GDP remained lower under the TNCs' ownership of the mines. The contribution of manufacturing was 11.1% in 2006 according to World Bank figures (10.5%, CSO), at the height of the copper price boom, compared to the 1997 level of 13.2% (11.8%, CSO) (World Bank, 2009; Central Statistical Office, 2008). The decline in the contribution of manufacturing to GDP during the copper price boom, together with the weaker correspondence between local manufacturing and mining growth rates (refer to Figure 4.3 of Chapter 4), reflect a poor linkage of the local manufacturing sector to mining under private ownership of the mines. These trends possibly portray practices of mining TNCs to replace several local companies with foreign companies in the supply of mining inputs.

Additionally, although a short spike occurred in manufacturing employment in the short term under private ownership to 67 752 in 2002, from the 2001 level of 47 679 and from the poor employment levels in the 1990s, manufacturing employment dropped sharply to 39 385 in 2003 (Figure 4.7 of Chapter 4). The steep decline in employment further emphasises the point that TNCs did not promote sustainable development of the local manufacturing sector over the short term. In addition, the weak development of manufacturing backward linkages to the mining sector challenges the validity of the argument that better mining performance has a positive knock-on effect on the manufacturing sector (The Economist Intelligence Unit, 2002:34). Rather, the poor benefits to the local backward linkages to the mines affirm the arguments of Lewis (1982) and Auty (1993) that the capital nature of modern mining operations renders them heavily reliant on foreign capital with poor local production linkages. Instead of local backward-linked industries to mining, fiscal linkages are the strongest linkage between the mining sector and the national economy (cited in Cawood *et al.*, 2001:220, 221).

Private mining TNCs cite the inefficiencies of local suppliers, particularly lower technical standards and quality, poor capacity for timely deliveries and lack of price competitiveness of products and services of local companies as the major motivations behind their decisions to opt for foreign suppliers (World Bank, 2002b:26; Transparency International, 2002:6). The cyclical problems[562] linked to difficulties in meeting supplies and in stockholding that local companies experienced further encouraged the foreign sourcing of goods (Fraser & Lungu, 2007:59). The withdrawal of Anglo American from Zambia before the commencement of the local business unit that would have assisted future retrenchees of these companies to develop businesses, to which KCM might have contracted work,[563] precluded greater benefits for local businesses. Certain weaknesses in government policies, elaborated upon in Section 6.5.1, especially the lack of an effective industrial policy to promote local suppliers under the ownership of mining TNCs, further contributed to the undermining of local suppliers and to their limited gains from the participation of mining TNCs in the economy.

[562] For instance, once overlooked, local companies would be discouraged from stocking the goods that mining TNCs required, which in turn diminished their capacity to meet subsequent short notice demands from multinational companies, again reinforcing the reluctance of mining TNCs to source inputs locally.
[563] Interview with Charles Muchimba, 18 November 2003.

6.3.4.2 Local workers

The reopening of the mines that had been closed improved employment opportunities at these mines. For instance, employment at Chambishi Non-Ferrous Metals increased from a skeleton staff of only 130 employees before the mines were privatised, to 537 workers in 2006 that were directly employed at NFCA. The total permanent and non-permanent employees at NFCA increased to 1 200 in 2003, at a time when the company was running at half capacity,[564] and rose further in 2006 to a total of about 2 100 employees that were also employed in subcontracting firms (Fraser & Lungu, 2007:48). Moreover, the opening of Bwana Mkubwa enabled the employment of 200 permanent local workers at the facility in 2003 and 640 workers were employed at Chambishi Metals under AVMIN that increased further to 660 employees in 2003, after the smelter was built (Lungu, 2001:16).[565]

However, notwithstanding the higher employment levels in the mines that reopened, the overall employment levels, particularly permanent employment dropped far below the 1990s' levels, when many mineworkers were also retrenched, under government ownership (elaborated upon in Section 5.4.2 of Chapter 5). Permanent employment levels in the mining sector declined dramatically, from 47 700 in 1996 before the copper mines were privatised to 22 000 in 2000, when all the mines were privatised, to only 19 000 in 2002 (refer to Figure 4.7 of Chapter 4). The more recent marginal increases in permanent employment levels, to 19 900 in 2004 and to 21 000 in 2006, were seemingly mainly because of the improved performance of the mines, following huge hikes in copper prices from 80.3 US cents/lb in 2003 to 305.6 US cents/lb in 2006 (The Economist Intelligence Unit, 2007b:31).

The increasing shift in the employment of mineworkers under private ownership of the mines from permanent to non-permanent employment further reduced greater advantages to workers. The non-permanent workers include those employed in external contract firms, fixed-term workers and casual workers, comprising 47% of the total mining sector labour force in Zambia in 2006. As noted in Section 5.4.2 of Chapter 5,

[564] Interview with Yu Zhongqin, 4 November 2003.
[565] Interview with Chama Kapambwe, 11 November 2003.

the poorer conditions of employment that non-permanent workers endure limit the benefits to local workers from the more recent increases in mining sector employment.

Advantages to local workers are further lowered through the tendency of external contractors to employ many foreign workers, especially from South Africa and from Zimbabwe, for semi-skilled work[566] as well as for unskilled work.[567] This was done despite the availability of highly skilled, semi-skilled and unskilled unemployed workers in Zambia. AVMIN employed mainly unskilled South African workers in the building of the Chambishi smelter at Chambishi Metals (Lungu, 2001:16).[568] Only 52 Zambian mineworkers, compared to 180 Chinese workers, were employed on permanent contracts at NFCA in 2006 reducing the benefits to Zambians of increased employment at the company (Fraser & Lungu, 2007:49).

In contrast, the pro-worker policies of the Kaunda government motivated by its electoral-maximising motives favoured higher employment levels, over the *x*-efficiency measures of mining TNCs that encourage a more streamlined workforce. However, continued high losses in the mines under government ownership might have manifested into even greater losses in employment in the mines than under private ownership and into zero employment within the highly pessimistic scenario of a closure of the mines, because of poor performance. The uncertainty as to what would have happened to the mining industry had the mines remained under government ownership precludes definitive judgment on the influence of changes in ownership of the mines to TNCs on the employment levels of workers in the mines.

Moreover, with the exception of KCM, CEC and J and W, expatriates (from countries of origin of the mining TNCs) were favoured to take over the senior positions under private ownership of the mines by TNCs.[569] This was the case despite the availability of well-trained and experienced Zambians that previously occupied many of the senior

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566 Such as bricklayers and security firms.
567 Interview with Tom Goodman, 18 December 2001.
568 Interview with David Chilipamushi, 17 December 2001.
569 Interviews with David Chilipamushi, 20 October 2003; Bernadette Mwakacheya, 17 October 2003; M. Shandavu, 10 October 2003; Wilphred Katoto, 12 November 2003; Dennis Wood, 21 October 2003 and Jack Jones, 22 October 2003.

technical[570] and managerial positions.[571] Under private ownership of the mines, expatriate managers are also paid much higher wages than local experts of similar qualifications and experience.[572] Under government ownership and management of the mines, highly qualified Zambians (fostered through 30 years of free education and through the Zambianisation policies, introduced during Kaunda's government) mostly dominated the senior management positions (Transparency International, 2002:6; Muchimba, 1998:29).

In some mining companies, expatriates make up almost the entire new management team, under TNCs' ownership of the mines. For instance, only one Zambian manager out of 12 was employed in management positions at NFCA in 2003, while the rest were from China (Fraser & Lungu, 2007:28, 57, 58).[573] Chibuluma Mines and Mopani[574] also employed mainly expatriates at higher management levels in 2003.[575]

However, CEC, KCM and J and W were more conscientious about employing Zambians at management levels. CEC employed only two foreign managers out of seven senior managers by 2003 and KCM, under the majority control of Anglo American, also retained most of the Zambian executives and managers[576] and brought in very few expatriates[577] (World Bank, 2002b:27).[578] Furthermore, in contrast to AVMIN that employed mainly foreign managers, J and W placed Zambians in top positions when it took over Chambishi Metals from AVMIN in late 2003 (Kaunda, 2002:166).[579] Additionally, Vedanta Resources brought in Indian management wholesale at KCM in 2004, but subsequently lowered the number of expatriates in the company (Fraser & Lungu, 2007:58).

570 Such as metallurgical engineers.
571 Interview with John Lungu, 12 November 2003.
572 Interview with Emmanuel Mutati, 18 November 2003.
573 Interviews with Charles Muchimba, 18 November 2003 and Yu Zhongqin, 4 November 2003.
574 With the exception of the Vice President, who is Zambian.
575 Interview with Charles Muchimba, 18 November 2003.
576 Including the Vice President, the Director of Finances, the Company Secretary, the Director of Public Relations and the Director of Human Resources at KCM (interviews with M. Shandavu, 10 October 2003 and Charles Muchimba, 18 November 2003).
577 Such as the Chief Executive Officer, the Chief Financial Officer and the Chief Operations Officers.
578 Interview with Francis Kaunda, 20 October 2003.
579 Interview with Agnes Bwalya, 9 November 2003.

Notwithstanding that it is an international practice of foreign investors to appoint employees of choice in key managerial positions, to maintain technical control of their operations, the selection of expatriates in preference to equally qualified Zambians prevents greater development of local capacities from the participation of mining TNCs in the economy. Also, the above discussion shows that some foreign mining investors also appointed expatriates in non-key positions. The absence of limitations on the contract period and on the number of times an expatriate can renew his/her contract,[580] together with the fact that expatriates in Zambia are paid twenty or more times the salary of Zambians with similar qualifications, encourages expatriates to adopt measures ensuring their continued stay in the mining companies (Regional Investor Survey, 2001:42; Muchimba, 1998:30).

Insufficient investments in the training of local Zambians by several mining companies, which are often confined to small-scale in-house training of employees, further limited the potential benefits that TNCs hold in developing the human capital of Zambians, through the transferring of skills to the host country. However, CEC stands out as having provided an effective retraining and replacement programme for its redundant employees, at a cost of US$400 000 and committed a further US$0.25 million for overseas training of Zambians in the first year of its operations in Zambia.[581] The retraining programme culminated into the establishment of almost 40 companies, owned and operated by former employees of the Power Division. CEC contracted work to these companies that in turn provided employment to almost 250 people at the end of 2003.[582]

More recently, Vedanta Resources also trained 40-50 Zambian business leaders on a management training scheme and employed Zambian staff in its international programme to gain international experience – the only company other than CEC to do so by 2006 (Fraser & Lungu, 2007:58). The training programme that Vedanta Resources provided enabled the company to reduce its expatriate managers. The

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580 Unlike the case in Zimbabwe and Botswana.
581 Interviews with Gary Loop, 29 October 2003 and Francis Kaunda, 20 October 2003.
582 Interview with Gary Loop, 29 October 2003.

company further re-established a similar training scheme to what was undertaken under the ZCCM, including the recruitment of 1 200 school leavers throughout the country to be trained and with the potential of working at KCM (Fraser & Lungu, 2007:58). The skills training provided in general supervision, motivation, expertise and safety promoted the human capital development of employees at KCM.[583]

However, the refusal of most mining companies to assume responsibility for non-core facilities, including the educational facilities of the ZCCM, greatly lowered the development of the human capital of the Copperbelt community. In contrast, under government ownership of the mines during Kaunda's government, the redistribution of mining surpluses[584] also for improving the social services of Zambians, including educational facilities provided by the ZCCM, greatly benefited among others the human capital development of the Copperbelt community. Also, loopholes in laws and particularly, poor implementation of laws protecting local workers (detailed in Section 6.5.1) further facilitated their replacement by foreign workers and suppliers and enabled the importing of jobs.

The practice of TNCs to substitute local capital limits the scope of the arguments of neo-classical proponents and neo-fundamentalists that TNCs complement local capital and reduce dependence. Rather, these activities support the views of neo-imperialists and Global Reach proponents that TNCs displace indigenous capital. This would likely reduce the most profitable local capital, the local bourgeoisie, into a 'comprador' or a dependent bourgeoisie, incapable of playing its historic role of promoting capitalist development, according to neo-imperialists (cited in Jenkins, 1987:29). The substitutions also affected local production adversely and generate an externally dependent economy, as is argued by Helleiner (1989:1454) and Padayachee (1995:14).

From the above discussion it is evident that within a weak state, returns to the Zambian economy from the extraction of copper under the TNCs' ownership of the mines became highly limited. Rather, certain opportunistic activities of mining TNCs, enabled

583 Interview with Norman Mbazima, 18 December 2001.
584 Mainly deposited with the BoZ.

through their stronger bargaining edge over the Zambian government, had a negative impact on the Zambian economy. The high concessions that mining TNCs for the most part continue to enjoy greatly reduced government tax revenue from mining. This, together with the repatriation of profits out of Zambia, limited a greater optimising of returns from the rent element of mining under TNCs' ownership of the mines. The meagre mining surpluses that the government was able to capture under private ownership also lowered the options of the country for saving and for accumulating foreign currency reserves from mining. In the context of the finite benefits that pertain to mining, as a non-renewable resource and because of the short life-spans of some of the mines, the granting of especially long-term concessions to mining companies seems highly illogical.

Moreover, the poor reinvestment of rent from mineral extraction to develop non-exhaustible sectors as well obstructed diversification and more sustainable development of the Zambian economy from mining surpluses. These also restricted higher employment levels. The practices of most mining TNCs to increasingly replace local suppliers and workers with foreign capacities further fuelled these trends. The combined effect of taxation and spending represents an important avenue through which a more equitable distribution of income from mining becomes possible (Volkerink, 2009:3).

The poor returns from mining, the lack of redistribution of the surpluses from mining and the high repatriation of revenue from mining out of Zambia under TNCs' ownership of the mines somewhat discredit the neo-classical argument that TNCs supplement the resources, foreign exchange earnings and local savings of Third World host countries. Instead, these weaknesses support the argument of neo-imperialists that TNCs drain the surpluses of host countries. This impedes capital accumulation that is essential for economic progress and contributes to the 'underdevelopment' of Third World host countries, according to these theorists (Helleiner, 1989:1453; Jenkins, 1987:27, 28, 29). The poor development consequences of these activities of mining TNCs also confirm the 'resource curse' argument that resource-abundant economies tend to grow less rapidly than resource-scarce economies. However, the poor capacity of the government greatly facilitated these outcomes.

6.4 FACTORS THAT INFLUENCED THE DECISIONS OF MINING TNCs TO DEPART FROM ZAMBIA

Regardless of the excessive concessions, probable transfer pricing practices and the ability of TNCs to use foreign suppliers, Anglo American and AVMIN nevertheless departed from Zambia, raising important questions as to the factors that influence the locational decisions of TNCs. The investigation below of the factors that accounted for the departure of these two mining companies from Zambia provides insight as to the locational decisions of mining TNCs.

6.4.1 Anglo American

Anglo American withdrew within 18 months of beginning its operations at KCM, announced on 24 January 2002, before it was to commence committing US$523 million for KDMP and to start paying, as agreed in its sale agreement, the US$60 million deferred cash consideration (payable in six monthly instalments, starting on 1 January 2006) (Zambia Daily Mail, 2002:3).[585] Anglo American cited financial losses as the key reason for its decision to suspend trading in ZCI shares and to depart from KCM. Technical problems and a higher than estimated cost of production and investment required for implementing the rehabilitation programme[586] also accounted for the poorer performance of KCM (The Economist, 2002b:1, 59; Craig, 2002:366; World Bank, 2003b:132, 2002a:4, 7, 26). KCM experienced heavy losses that amounted to about US$l08 million in the 21 months ending December 2001, and US$159.9 million for the year ending 31 December 2002.

A failure to secure non-recourse project funding on reasonable commercial terms,[587] through commercial borrowing from capital markets and from shareholders for its key project, KDMP, also seems a major reason for the departure of Anglo American. The cost of construction of KDMP was then estimated between US$500 million and

[585] Interview with L. M. Lishomwa, 29 October 2003.
[586] Largely because the delay in the rehabilitation was accompanied by a looting of the mines, stripping of machinery, rusting of vehicles and a flooding of shafts.
[587] Without recourse to shareholder guarantees.

US$1 billion (Craig, 2002:365, 366; The Economist, 2002b:1, 2; World Bank, 2002a:2, 26; Times of Zambia, 2002:2; Kaunda, 2002:184, 187). The funding problems that Anglo American experienced were caused by the inability of ZCI to provide further funding to KCM, beyond its obligations under the Shareholders Subscription and Loan Agreement, over and above US$370 million in commitments that have already been given by shareholders (Kaunda, 2002:184; Ministry of Mines and Mineral Development, 2003:5; Craig, 2002:366; Zambia Daily Mail, 2002:3).[588] The government was also unable to secure the concessional funding from the World Bank that Anglo American requested to assist it in its mining operations in Zambia (World Bank, 2002a:26).

Furthermore, the losses that Anglo American experienced at KCM rendered the company's strategy, viz. to finance a significant proportion of the cost of developing KDMP mainly from cobalt proceeds from existing operations at the Nchanga open pit,[589] unfeasible (Craig, 2002:365, 366; The Economist, 2002b:1; Kaunda, 2002:186; World Bank, 2003b:132, 2002a:6, 26; Africa Research Bulletin, 2003b:15601). Without KDMP, an enormous greenfield copper project that would have ensured the continuation of copper mining in Zambia and its re-establishment as a major copper mining country, further investment in KCM, with its small, difficult and short lifespan, would unlikely have produced the required rate of return acceptable to Anglo American (Kaunda, 2002:184; World Bank, 2002a:7; Times of Zambia, 2002:2). The copper price that reached less than US$400/ton in 2001 needed to exceed US$1 700/ton for a period of 12 months before it would have been feasible to proceed with KDMP (Africa Research Bulletin, 2001d:14977).

The poor copper prices that dropped from an average of 88 cents per pound in September 2000 to just under 60 cents per pound in November 2001, the lowest price in 15 years, also affected the performance of Anglo American in Zambia adversely (Ministry of Finance and National Planning, 2002c:63). However, the low copper prices

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[588] These funds were redeployed owing to losses that KCM experienced in the day-to-day operations of KCM, rather than for the development of the KDMP project for which these funds were intended.

[589] Estimated to contribute cash of about US$300 million.

alone do not appear a major reason for Anglo American's decision to pull out of Zambia, since smaller mining companies that would have been affected more by the poor copper prices did not withdraw from Zambia (The Economist, 2002a:59; Business in Africa, 2002:2; Business Day, 2002c; Mining News, 2002). Moreover, Anglo American's refusal to reverse its decision to withdraw, despite expectations of recovery in the price of copper, and its subsequent investment of US$1.3 billion in a copper mine in Chile shortly after its withdrawal from Zambia, regardless of the low copper price, further discredit this argument.

Anglo American also cited the poor grading of ZCI in the base metal division on a global risk return basis, under its then CEO, Tony Trahar, as a further reason for its decision to exit from Zambia (Business Day, 2002a; Business Day, 2002b). In 2001, the base metal division experienced losses of US$19 million, with ZCI in Zambia and Anaconda Nickel in Australia carrying particularly high risks, which reduced Anglo American's global competitiveness in the base metal division. An increase of only 7.3% in Anglo American's shares in 2001 made it the worst performer of the six-member Bloomberg Europe Metal and Mining Index (Bloomberg, cited in The Star, 2002a; Business Day, 2002a).

However, the global objective of its shareholders in London to diversify away from Africa appears to be a more plausible reason for Anglo American's departure from Zambia than low copper prices and a decision to get out of base metals.[590] This is mirrored in the fact that Anglo American invested in the copper mines in Chile almost immediately after its departure from KCM. Anglo American's shareholders in the transformed board in London, which largely consisted of members unconnected to Southern Africa, blamed negative risk perceptions of investments in Africa for the lower share prices suffered by Anglo American,[591] who possessed significant investments in Africa (Kaunda, 2002:187).[592]

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590 To focus on different minerals to spread the risks associated with price changes.
591 Over bigger mining companies, such as Rio Tinto.
592 Interviews with Simon Capper, 30 October 2003 and Sipho Phiri, 30 October 2003.

The relocation of Anglo American's headquarter or its primary listings from Johannesburg to London in 1999 and the decision of Anglo American to sell the 35% shares it had bought from AVMIN[593] in Zambia, somewhat vindicate the argument that Anglo American intended to reduce its portfolio in Africa[594] and to shed its 'regional' image (Kaunda, 2002:187; Africa Confidential, 2002:1; The Economist, 2002a:59). The less favourable attitude of the shareholders towards investments in Africa was also behind the board's vetoing thrice the decision for Anglo American's re-entry into Zambia's mining industry during the privatisation of the ZCCM, before it was finally passed (Kaunda, 2002:187). Moreover, the greater short-term profit-maximisation motives of the new board members further influenced the exit strategy of Anglo American. The decisions of the new board members represented a change from decisions of founding members of Anglo American, the Oppenheimers, who previously also based decisions to some extent on sentiments towards Zambia's mines[595] and on longer-term mining investments in Africa (Kaunda, 2002:187).

However, higher returns on investment in the Chilean mines over those of Zambia also contributed to the decisions of Anglo American to shift its mining investments to Chile (The Economist, 2002b:1; Africa Research Bulletin, 2003a:15551). The higher returns were primarily because of the lower copper production costs at an average of 50 cents per pound at the Chilean mines, enabling the achievements of profit even when the copper price dropped to 62 cents per pound.[596] Mining in the South American countries have additional advantages over Zambia that render them more attractive to investors.

These include:

- the higher transport costs of Zambia as a landlocked country (1 860 km from the closest port);
- the open-cast mining, prevalent in South American countries, that lowers the costs of mining porphyry ore bodies, while the deeper sedimentary ore bodies prevalent in

[593] Some believe the purchase of AVMIN's shares constituted an avenue to facilitate Anglo's return to Zambia once it freed itself of its onerous obligations through its withdrawal from Zambia.
[594] Interview with Simon Capper, 30 October 2003.
[595] Interviews with John Lungu, 12 November 2003 and Dave Phiri, 23 October 2003.
[596] Interview with John Lungu, 12 November 2003.

Zambian mines necessitate underground mines;[597]

- the superior infrastructure of Chile in comparison to that of Zambia, accounting for its greater cost competitiveness (Kaunda, 2002:188); and
- the conflicts in the neighbouring Congo and Zimbabwe.[598]

Accordingly, notwithstanding the extensive concessions that it enjoyed in Zambia and the stricter regulatory framework for mining TNCs in Chile, Anglo American withdrew from KCM in Zambia and subsequently invested in the more cost-effective Chilean copper mines. Also, the government was unable to attract a suitable investor for KCM until the end of 2004, after Anglo American left in 2002. The lack of an exit clause, as well as the failure of government policies to ensure higher sunk costs from mining TNCs and the weak enforcement of legislation further facilitated the withdrawal of Anglo American from Zambia.

6.4.2 AVMIN

Liquidity problems, high costs and its failure to win the bid for the Luanshya/Baluba mines largely accounted for AVMIN's departure from Chambishi Metals in 2002. Low cobalt prices of between US$5.9 and US$7 per pound in 2002,[599] high costs associated with the refurbishing of its smelter, a US$104 million impairment charge and limitations that the South African Reserve Bank placed on the amount of money AVMIN could send out of South Africa greatly contributed to the liquidity problems of the company (Africa Research Bulletin, 2003b:15601).

The high costs of production were mainly owing to AVMIN having to replace a faulty smelter in 2002.[600] Technical problems at its main furnace and smelter and the poor design of the new plant that AVMIN built for treating the smelter slag dump added to the costs of the company. These factors contributed to Chambishi Metals' experiencing losses of US$195 million in 2002 that exacerbated the company's already onerous debt

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597 Despite these being of a higher grade.
598 Interview with Zion Simwanza, December 2003.
599 Following decreases in orders for jets after 11 September 2001 (interview with Chama Kapambwe, 11 November 2003).
600 Which resulted in the copper coolers taking much longer at 18 months to rectify, than the six months it envisaged (interview with Chama Kapambwe, 11 November 2003).

service burden (The Economist, 2002a:59; Africa Mining Intelligence, 2003b:3; Africa Analysis, 2003a:16; World Bank, 2003b:132).[601] The high debt of the company obstructed the construction of a US$l0 million cobalt solvent extraction plant (Africa Research Bulletin, 2003b:15600-15601).

An unsuccessful bid for the Luanshya/Baluba Mines further contributed to its decision to withdraw from Zambia.[602] The good ore grades of the Luanshya/Baluba mines that require less refinement would have supplemented the company's production, lowered AVMIN's costs of production[603] and promoted its longer-term sustainable production (Sittard, cited in Times of Zambia, 2003:1; Africa Research Bulletin, 2003b:15600).[604] Since the long-term viability of Chambishi Metals was dependent on its obtaining cheaper copper ores,[605] it was logical for AVMIN to sell its shares in Chambishi to J and W Holdings, following the success of the latter company in securing the bid[606] for the Luanshya/Baluba mines.[607] AVMIN was forced to write down US$135 million (half the value of its Zambian operations) on its balance sheet in 2002 (World Bank, 2003b:132; The Economist Intelligence Unit, 2002:42).

The above discussion shows that locational decisions of Anglo American were not significantly influenced by concessions and liberalised policies as the company withdrew from Zambia despite all the concessions it enjoyed. Economic factors, especially the competitiveness of the country in relation to other countries, determined through global profit-maximising motives of the mining TNCs and the location and quality of minerals in the mining sector, proved overwhelming in determining the locational decisions of Anglo American. Factors accounting for the lower competitiveness of Zambia in relation to Chile were a high-risk perception of its

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601 Interview with Chama Kapambwe, 11 November 2003.
602 That AVMIN banked on to supply it with copper and cobalt concentrate that would have ensured a more sustainable existence for Chambishi Metals.
603 Interviews with Chama Kapambwe, 11 November 2003; Silane Mwenechanya, 24 October 2003; M. Shandavu, 10 October 2003 and Andrew Sardanis, 19 October 2003.
604 Interview with Stuart Cruickshank, 28 October 2003.
605 Which would have been possible if AVMIN had won the Luanshya/Baluba bid.
606 Rumours of an on-going agreement between AVMIN and J & W to eventually sell Luanshya/Baluba and Chambishi to J & W once it won ownership of Luanshya/Baluba at a great profit led to the government short-circuiting the process by allocating Luanshya/Baluba to J & W instead of to AVMIN (interview with Silane Mwenechanya, 24 October 2003).
607 Interviews with Stuart Cruickshank, 28 October 2003, Fortune Kamusaki, 25 November 2003, Silane Mwenechanya, 24 October 2003; M. Shandavu, 10 October 2003 and Andrew Sardanis, 19 October 2003.

shareholders of African investments, the relatively high costs of production and the greater inaccessibility of copper from deep-level mining in Zambia over the open-cast mining that is prevalent in Chile.

Moreover, losses and liquidity problems common to both Anglo American and AVMIN further contributed to their departure from Zambia. The poor prospects of the long-term feasibility of Chambishi Metals subsequent to its failure to win the Luanshya/Baluba bid also proved highly significant in influencing AVMIN's decision to depart. The limited influence of concessions, liberal policies and more restrictive economic policies of the Chilean government on the locational decisions of Anglo American is in line with the argument of Chang (1998:240) that concessions and liberal policies are not a guarantee for sustainable investment. It also vindicates the finding of a number of studies that concessions would not necessarily lead to more Foreign Direct Investment (FDI). Rather, they serve merely to lessen the net value of investments made by mining TNCs that would likely have been made in any case, even in the absence of the concessions (Action Aid International *et al*., 2009:25).

It further supports the argument of Padayachee (1995:166) that tax incentives, tax holidays and differentiated structures prove less important than factors such as the general investment climate and policies affecting specific sectors in attracting foreign investment. The significant influences of the competitiveness of the country in relation to others and the quality of minerals on the locational decisions of Anglo American and AVMIN confirm the argument of Helleiner (1989:1461) that the location and quality of minerals prove especially important in determining the locational decisions of TNCs in the mineral sector.

6.5 THE POLITICAL-ECONOMIC IMPLICATIONS OF GOVERNMENT REGULATORY AND INSTITUTIONAL CAPACITIES CONTROLLING MINING TNCs AND OF TNCs' ACTIVITIES IN THE MINING SECTOR

It is evident from the above discussion that various weaknesses in the public sector and loopholes in the enforcement of regulations affecting mining TNCs greatly contributed to the poorer gains of the government under private TNCs' ownership of the mines.

Several theorists stress the importance of strong institutions and effective legislative measures in regulating of the activities of TNCs, discussed in Chapter 3.

In particular, strong institutional capacities are necessary to protect the interests of the nation against some of the activities of TNCs, to ensure that the greatest possible share of the rent element from mining accrues to the host country, and to promote more beneficial outcomes from mining in resource-abundant economies (see, for example, Padyachee, 1995:166; Chang, 1998:238; Action Aid International *et al*., 2009:x; Bebbington *et al*., 2008:10). Criteria that enhanced the capacity of developmental states, according to developmental theorists (but also relevant to mining economies) are economic bureaucracies that enjoy power and competence and are insulated, a state that has a corporatist role and effective industrial policies (see, for example, Leftwich, 1995, Chang, 1993, 1994, Amsden, 1989, 1997). The formidable institutional and state capacities of developmental states enable them to direct the activities of TNCs towards more advantageous outcomes for the host country.

Broadly, Section 6.5 examines and assesses first the capacities of various regulatory and institutional measures and the monitoring and enforcement capacity of the government in controlling and directing the activities of mining TNCs and their political-economic consequences. The political-economic implications of the activities of TNCs in the mining sector are then considered.

6.5.1 Political economy and assessment of capacities of regulatory and institutional measures controlling the activities of mining TNCs

Table A10 (in the Annexure), lists the main legal measures established to regulate the operations of private companies since Chiluba's rule, which also apply to mining TNCs. The various institutional and regulatory measures for controlling and monitoring the activities of private mining companies in Zambia during Chiluba's government broadly encompass government regulatory measures, bilateral agreements between the government and the private mining companies and the various government bodies commissioned to monitor private sector activities.

The principal measures that specifically regulate the activities of mining companies under private TNCs' ownership entail the Investment Act, the Mines and Minerals Act and the development agreements. Government measures that seem necessary to control and ensure more beneficial outcomes from the activities of mining TNCs in Zambia are also investigated. These include: (i) legal measures regulating bankruptcy and the securities and exchange in Zambia; (ii) measures to protect both the mineworkers and local suppliers against certain activities of TNCs and to direct the activities of TNCs towards more beneficial outcomes for local capacities; (iii) statutory provisions to enforce payments of exit damages by TNCs, should they withdraw from Zambia; (iv) government measures to encourage greater investments and higher sunk costs from mining TNCs; and (v) measures to curb instability in the foreign exchange market.

6.5.1.1 Investment Act (1995) and the Mines and Minerals Development Act (1995)

The reforms of the Investment Act of 1995 and of the Mines and Minerals Development Act of 1995 were the most significant policy changes established to accommodate the activities of private companies and of the mining sector respectively. These reforms, largely driven by the IMF and the World Bank, altered many of the measures that the state had previously established to control the activities of companies (Fraser & Lungu, 2007:3, 11). The poor bargaining leverage of the Zambian government, and the economy's high dependence on aid forced the government to adopt these reforms. The World Bank made the reforms conditional on the release of the Privatisation and Industrial Reform Credit (PIRC) 11 loan of 1993.

The reforms introduced in the Investment Act of 1995 and in the Mines and Minerals Development Act of 1995[608] were highly favourable to foreign investors in mining, by way of special incentives.[609] The incentives specified in the Investment Act provided further assurances against nationalisation and eliminated foreign exchange controls.[610]

[608] That superseded the Mines and Minerals Act of 1972.

[609] Special incentives were also granted to the Multi-Facility Economic Zone (MFEZ), at Chambishi, specified in the 2007 budget, through which they would receive various tax incentives. A number of Chinese companies, expected to create 60 000 new jobs in Chambishi, are likely to be the first to take advantage of the facility.

[610] Via the Zambian Investment Centre (ZIC).

The elimination of foreign exchange still enables foreign companies to repatriate all funds in respect of dividends, principal and interest on foreign loans, management fees and other charges (The Economist Intelligence Unit, 2007b:29, 38). However, the exclusion of local investors from these concessions undermined local suppliers to the mines.[611]

Moreover, incentives granted under the Mines and Minerals Development Act of 1995 considerably reduced the income tax returns to the government from mining companies. These concessions entailed deducting the investments made in the mining sector from taxes and exempting mining companies from customs duties on imported machinery and equipment. Provisions of the Act also entitled specific companies to enter into bilateral 'development agreements' with the government. The bilateral agreements enabled mining TNCs to gain additional incentives to those granted by the Act (Fraser & Lungu, 2007:11). The incentives that both of the Acts granted to the mining TNCs and the concession allowing bilateral agreements to override the provisions of the Mines and Minerals Development Act were highly favourable to the mining TNCs. Conversely, these incentives disadvantaged the local entrepreneurs (Fraser & Lungu, 2007:11).

The various concessions granted under both of the Acts greatly reduced government revenue obtainable from foreign mining TNCs (as is noted in Section 6.3.1) limiting the gains to the government from the rent element of mining. The concessions amount, in various ways, to the government's subsidising the operations of TNCs in Zambia. However, the more recent adoption of the Zambia Development Agency Act of 2006 (executed under the Zambia Development Agency (ZDA)[612] established in 2007), which replaced the Investment Act of 1995, aims to raise the profile of manufacturing companies and to eliminate discrimination between local and foreign manufacturing companies, which existed in the Investment Act. The ZDA Act further restricts the scope for incentives and makes it more difficult to employ foreign workers (Ministry of

611 Interviews with Ladslous Mwansa, 7 October 2003 and Alick Lungu, 14 October 2003.

612 The ZDA was to act as a one-stop shop for investors to promote more efficient awarding of licenses for starting businesses in Zambia. The ZDA consists of an amalgamation of the ZIC, the Export Board of Zambia, the ZPA, the Zambia Export and Processing Zones and the Small Enterprise Development Board.

Mines and Mineral Development, 2003:4; The Post, 2003b:4; United Nations Conference on Trade and Development, 2006:15; The Economist Intelligence Unit, 2007b:38). Moreover, the higher taxes that the amendments to the Mines and Minerals Development Act that came into force in 2008 impose on mining TNCs would promote more favourable outcomes for the Zambian economy (Bloomberg, 2008, cited in The Zambian Chronicle, 2008).

6.5.1.2 Development agreements

Similarly, within the development agreements that entail bilateral agreements between the government and the mining companies, the dominant bargaining position of TNCs over the Zambian government enabled them to negotiate highly beneficial terms for themselves. These terms were often at the expense of the Zambian economy, demonstrating that within an unequal bargaining relation bilateral agreements tend to favour the stronger party. Additional pressure that the government faced from donors to swiftly privatise the final assets of the ZCCM enabled the mining companies that were later privatised to negotiate for additional concessions to those granted to earlier privatised companies.

Within the development agreements the mining TNCs were able to further reduce the royalty tax rates, from the 3% of the net back value of the minerals produced, specified in the Mines and Minerals Development Act of 1995 (Fraser & Lungu, 2007:11). The legislation of certain terms of the development agreements of KCM and MCM, making external arbitration possible in the event of a breach of these terms, ensured a stable physical environment for mining investors. A stable environment promotes investor confidence that is favourable to mining TNCs.[613] On the other hand, the legislation of clauses of the development agreements, including those allowing for concessions, renders it difficult to make changes to these agreements, to ensure more favourable outcomes for Zambia.

[613] Interviews with Silane Mwenechanya, 24 October 2003 and Chama Kapambwe, 11 November 2003.

6.5.1.3 Bankruptcy laws and regulations controlling securities and exchange

The laws that the Zambian government established to cover bankruptcies of companies and to regulate securities and exchange, which is important in a privatised setting for achieving greater efficiency and equity, have however proved inefficient (Stiglitz, 1998:19 and 20).[614] The bankruptcy laws that shield the liquidated companies from paying terminal benefits to workers further favoured mining TNCs, but disadvantaged the workers.[615] The Securities and Exchange Commission in Zambia also has various shortcomings and is in need of further revision.[616]

Despite the various measures introduced through the banking system to curb money laundering, detection of money laundering becomes difficult when money transactions take place on a cash basis outside the banks. International effort is required for more effective monitoring of money laundering.[617] Poor monitoring over securities and exchange, in the absence of exchange controls, facilitated the repatriation of resources out of Zambia, also from mining TNCs. This affected the Zambian economy in a negative fashion, in loss revenue.[618]

6.5.1.4 Measures to protect mineworkers against malpractices by TNCs

Poor implementation of several labour regulations and of certain clauses in the development agreement on aspects of the training of local Zambians is a major weakness in measures to protect mineworkers.[619] Fear on the part of the government that increasing demands on powerful mining TNCs may discourage foreign investment greatly contributed to the poor implementation of regulations protecting mineworkers.

Significant reductions of the labour force and other measures that render it more difficult to organise collective action have reduced the capacity of Zambian workers to demand better working conditions. Under the TNCs' ownership of the mines, the mine

614 Interview with Danny Kalyalya, 31 October 2003.
615 Interview with John Kangwa, 21 November 2003.
616 Interviews with Danny Kalyalya, 31 October 2003; Jack Jones, 22 October 2003; John Kangwa, 21 November 2003 and John Lungu, 12 November 2003.
617 Interviews with David Chilipamushi, 20 October 2003 and John Lungu, 12 November 2003.
618 A tribunal, which would have been more independent of the government and which would have been a less costly option for Zambian taxpayers, might likely have been a better alternative than the Task Force for investigating corruption in Zambia.
619 Interviews with Fred M'muembe, 14 October 2003 and Honourable Eugene Appel, 24 November 2003.

unions that possessed significant power during Kaunda's government consisted by 2006/2007 of only 16 000 members at the MUZ and 4 000 to 5 000 members at the National Union of Miners and Allied Workers (NUMAW) (Fraser & Lungu, 2007:24, 26, 52). Several strategies of mining TNCs that undermine effective operations of trade unions are contrary to the Industrial and Labour Relations Act and the International Labour Organisation (ILO) conventions that prohibit practices curtailing the unionisation of workers.

Moreover, poor enforcement of the provision of the Investment Act that only professional people may be recruited from outside Zambia[620] and then only if the skills are unavailable in the country, which also limits the employment of expatriates, have hindered greater participation of Zambians at higher levels. These omissions enabled the external contract companies that the mining TNCs enlisted, to employ many foreign unskilled and semi-skilled workers (World Bank, 2002b:27 and Committee on Economic Affairs and Labour, 2000:17, 44).[621] This also points to deficiencies in the Ministry of Labour in the control of work permits. The absence of clauses in the development agreements promoting greater participation of Zambians in the management of private mining companies,[622] further curtailed their participation, even though many Zambians possessed the required skills.[623]

Furthermore, the non-obligatory nature of the clauses in the development agreements that refer to training, financial assistance to aid the retrenched workers in gaining alternative skills and succession charts for employing local workers limits the enforcement capacity of the Zambianisation Committee, established to oversee the training of Zambians.[624] These omissions also reduced the employability of those that lost their jobs.[625] Additionally, the precedence given to development agreements that largely promote the interests of mining TNCs, over the provisions of the Safes

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620 Interview with Honourable Eugene Appel, 24 November 2003.
621 Interviews with David Chilipamushi, 20 October 2003 and Wilphred Katoto, 12 November 2003.
622 Deemed the prerogatives of the respective boards of private companies (interview with Charles Muchimba, 18 November 2003).
623 Interview with M. Shandavu, 10 October 2003.
624 Interviews with Francis Kaunda, 20 October 2003; Chama Kapambwe, 11 November 2003; Jack Jones, 22 October 2003; Andrew Hickman, 7 November 2003 and Emmanuel Mutati, 18 November 2003.
625 Interview with Emmanuel Mutati, 18 November 2003.

Agreement that the ZPA employed for the privatisation of non-mining assets, has proven less beneficial to the local mining community. The Safes Agreement provides for explicit commitments to promoting Zambia's interests, including those of the employees. The provisions of the Safes Agreement typically covers conditions of service, training and development, the possibility of equity purchase by employees and other forms of employee involvement, plans for sourcing goods in Zambia, the sale of shares to Zambians and Zambian participation at management and board levels (ZPA, 2002:5).

The absence of government measures to ensure horizontal linkages between mining TNCs and local capacities that would reduce their reliance on expatriate employees further hindered significant development of Zambia's human capital that such linkages potentially hold for the host country (see, for example, Evans, 1998; Kozul-Wright, 1995:150, 153; Padayachee, 1995:173), noted in Chapter 3 (Kaunda, 2002:176). The higher returns of human capital, which could translate into a dynamic comparative advantage for the host country together with the transfer of technology skills, hold greater returns than research and development in countries that are not operating at the technological frontier. This underscores the importance of building the human capital of developing countries, which is unlikely to be filled by the market (Stiglitz, 1998: 24, 25, 26, 32). While the mining sector still possessed a good level of residual middle-level skills up to 2001,[626] most investors expressed a concern as to the longer-term impact of the declining educational standards, lower levels of public health and of declining government efficiency on the future skills of Zambians (Regional Investor Survey, 2001:44). An adverse impact on the quality of human capital in the privatisation of SOEs, also through reduced training and worker health, would hinder growth (Pineda & Rodriguez, 2002, cited in Kirkpatrick & Parker, 2005:528).

Additionally, the poor capacity of the relevant formal bodies in implementing regulations protecting the safety standards of mineworkers undermined better safety standards for mineworkers. The measures established to protect the safety of workers

[626] Largely attributable to the achievements made by Kaunda's Zambianisation policies (Muchimba, 1998:29).

include the Mines and Minerals Environmental Regulations, the Mines Safety and Explosives Regulations, revised in 1996[627] and the Workers Compensation Act. The safety of workers is further monitored through the Mentor Council of Zambia.[628] The diminished capacity of mining trade unions to effectively execute their roles in regulating and pressurising for safer working conditions also limited higher safety standards for mineworkers. Building the capacities of the Department of Mining,[629] and of the inadequately funded Mines Safety Department[630] are important for ensuring more effective implementation of safety measures in the mines (Fraser & Lungu, 2007:24 and 26).

6.5.1.5 Measures to protect local suppliers against certain activities of TNCs and in directing TNCs' activities towards more beneficial outcomes for local capacities

Several weaknesses in the regulatory measures governing the relations between local suppliers and the mining TNCs under MMD rule disadvantaged local suppliers. Many of these loopholes though favoured foreign suppliers. Broadly, these weaknesses encompass firstly, the absence of effective measures to curb various activities of mining TNCs that prove harmful to local suppliers. Secondly, the government failed to establish an effective industrial policy to encourage the development of local suppliers to the mines under the ownership of mining TNCs. This was mainly owing to its weak bargaining position at the time that the mines were privatised enabling the IMF and the World Bank to pressurise the MMD government into adopting liberal policies and a foreign investor-friendly regulatory regime, ahead of the privatisation of the ZCCM.

The weaknesses in measures for curbing certain activities of TNCs[631] that harm local suppliers and manufacturers, while favouring foreign suppliers, encompass a failure of government measures to effectively address:

- Tendencies of TNCs to replace many Zambian backward-linked suppliers and firms

627 Largely owing to a lack of funds.
628 Interview with Andrew Hickman, 7 November 2003.
629 That initially provided detailed comments to encourage mining companies to meet their commitments but that neglected, subsequently, to do so. It also neglected to play its role in formulating regulations (Fraser & Lungu, 2007:26). The Department of Mining suffers from a shortage of legal draftsmen.
630 That is supposed to participate in the formulation of new regulations and to manage an inspections regime that would secure effective implementation of mining regulations (Fraser & Lungu, 2007:26).
631 Facilitated through liberalisation policies introduced by the Chiluba government.

to the mines with mainly South African firms in the supply of various mining inputs.[632]

- Alleged collaboration between the private managers of the mines and foreign suppliers of mining inputs.[633]
- Lack of transparency in the tendering process of suppliers, which tends to favour foreign companies.
- The poor capacity of local suppliers to the mines to comply with stringent procurement criteria of price competitiveness and International Organisation for Standardisation (ISO) 2000 standards that private mining companies employ.[634] The selection of suppliers is also largely based on their bank statements, auditors, premises, capacity and delivery time.[635]
- Alleged practices of TNCs of employing Zambians mainly as agents, rather than as partners to foreign support industries to the mines. Lack of collateral that constrains Zambian businesses from buying shares in multinational companies and the tendencies of some companies, which may start off in partnership with Zambians, to buy them out after some time, curtailed the development of Zambian businesses.
- Inclinations of foreign companies to merely set up small operations or representative offices in Zambia to supply the mines, instead of establishing manufacturing industries in the country.[636]
- Alleged tendencies of some multinational manufacturing companies to strip and to transfer the assets of their Zambian companies to their home countries, while converting the existing premises in Zambia merely into warehouses or storehouses.[637]

Secondly, the failure of the MMD government to introduce an effective industrial policy, also policies directing the activities of TNCs towards greater advantages for local suppliers, have deprived the country of substantial benefits that industrial policies

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[632] Such as chemicals and copper cables (interview with Eddy Kapungulya, 13 November 2003). The institutions differ from what was the case under government ownership of the mines, also under Chiluba's rule, during which time continued preference was still given to local suppliers (interview with Ladslous Mwansa, 7 October 2003).
[633] Interview with Honourable Eugene Appel, 24 November 2003.
[634] Interview with Alick Lungu, 14 October 2003.
[635] Interviews with Chama Kapambwe, 11 November 2003; Honourable Eugene Appel, 24 November 2003; Honourable Dipak Patel, 15 October 2003 and Emmanuel Mutati, 18 November 2003.
[636] Interview with Mark O' Donnell, 16 October 2003.
[637] Interview with Eddy Kapungulya, 13 November 2003.

hold for developing countries (Amsden, 1997:469 and 470). Industrial policies additional to those discussed in Section 4.2.2.1 but applicable specifically to the participation of mining TNCs in the economy, which would have had positive spin-offs for local industrial development, include in particular, the establishment of effective vertical and horizontal linkages between the global TNCs and local suppliers. Such linkages would have generated employment opportunities and led to the transfer of know-how (that would promote human resource capabilities of host countries). The linkages would also have transferred appropriate resources (including technology) to local suppliers and provided finance and managerial assistance to local firms (Gordon, 1994, cited in Padayachee, 1995:166; Kozul-Wright, 1998:150, 152, 153, 154).

Vertical linkages between local mining suppliers and mining TNCs that would have promoted the development of local capacities would further have limited the tendencies of TNCs to substitute local suppliers with foreign suppliers (Fraser & Lungu, 2007:4, 60). The absence of effective enforcement measures to promote local procurement also curtailed such benefits. However, more recently, the Mining Liaison Committee of the Chamber of Commerce negotiated with KCM to try and match the needs of the company[638] with the local manufacturers of goods (Fraser & Lungu, 2007:59). The new Development Agency Act of 2006 that encourages such a partnership[639] came into force only after many mining TNCs had already established their own suppliers and after many Zambian suppliers became bankrupt. Trade liberalisation policies contributed significantly to the bankruptcies of local companies.

Moreover, an industrial strategy to attract and support forward linkages in the mining sector in addition to smelting, including the production of electrical products in Zambia is necessary.[640] Incentives and a supply of a certain percentage of the copper cathodes that mining companies produce to local manufacturers that need copper inputs could also encourage the development of value-added industries to the mining sector (Fraser & Lungu, 2007:17, 60).

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638 Such as foundry, fabrication and machinery products.
639 Interview with Fred Yamba, 25 November 2003.
640 Namely copper wires, electrical plugs, pipes and other light industrial goods.

Furthermore, the failure to establish effective horizontal linkages or joint ventures between mining TNCs and local suppliers deprived Zambia of significant development of especially its human capital, through the transfer of valuable resources, technology know-how and training to local suppliers that such linkages hold for the economy. This would especially be the case if the research activities of global TNCs, particularly of deeper integrated production systems, include horizontal linkages with similar local industries that would have positive local spillover or externality effects (Padayachee, 1995:173). Horizontal linkages with local suppliers would further promote greater sustainability of local businesses if foreign companies decided to leave the country (World Bank 2002b:27).

Additionally, a failure to establish an industrial policy to protect and support local capacities, in the face of excessive foreign investor-friendly and liberal policies, elaborated in Section 4.2.2.1 of Chapter 4, favours foreign suppliers, whilst facilitating the substitution of local capacities in the supply of mining inputs. In Chapter 4 it is noted that in particular, trade liberalisation policies, at a time when Zambia's industries were weak and when markets were highly imperfect, precluded the development of an effective industrial strategy during Chiluba's government. Instead, the rapid influx of lower priced foreign equipment and of services firms, especially from more competitive South African firms[641] that free trade policies facilitated challenged the entry of local suppliers into the lucrative supply market of the mining sector (World Bank, 2002b:26; Regional Investor Survey, 2001:40). Duty exemptions on imported equipment granted to foreign companies but not extended to local companies, that reduces the incentive to source and build such facilities locally, are also favourable to foreign companies.

While donors pushed for liberal policies and a foreign investor-friendly regulatory regime in Zambia, they showed little interest in supporting productive investment in the Zambian economy or encouraging a transformation of its productive mode, which represents a rapid means of promoting development. A stronger capacity of local

[641] South Africa was Zambia's largest supplier in 2001 with 56.8%, with the United Kingdom at 8.3% in second place (Van Buren, 2003:1155).

industries in Zambia would also have improved the government's bargaining leverage to direct the activities of TNCs, as was the case with developmental states (Leftwich, 1995:417). On the contrary, the totally liberalised economy reduced the bargaining power of the government over those of the mining TNCs.

Ineffective monitoring and the omission by the appropriate committees to challenge the failure of private mining companies to implement local sourcing policies also curtailed more beneficial outcomes for local businesses from the privatisation of the mines (Fraser & Lungu, 2007:4, 17). Loopholes in agreements *obliging* mining TNCs to support local suppliers, alongside clauses in development agreements allowing companies to choose their own suppliers[642] and to freely move goods in and out of the country,[643] reduced the scope of plans in some development agreements[644] to transfer skills to Zambian majority businesses (Bwana Mkubwa Development Agreement, 2004:14). Other factors discussed in Section 4.2.2.1 of Chapter 4 and those listed in Table A7 (in Annexure) such as insufficient capital and the high costs of production of local suppliers further influenced suppliers adversely. These factors also need to be addressed to improve the competitiveness of local suppliers.

6.5.1.6 <u>Statutory provisions to enforce the payment of exit damages by TNCs</u>

The weak bargaining position of the Zambian government compared to mining TNCs that enabled TNCs to steer the bilateral development agreements in their favour contributed to the government's neglecting to impose exit damages or penalties on TNCs, should they withdraw from Zambia. The omission contributed considerably to the less generous terms that the government was able to extract from Anglo American at its departure, than what was expected (Business in Africa, 2002:2).[645] It further enabled Anglo American to threaten the withdrawal of the US$30 million it paid for KCM, should the Zambian government make further demands on the company (Mwanawasa, cited in Business in Africa, 2002:2). The absence of an exit clause in government

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642 Interview with Zion Simwanza, December 2003.

643 With minimal controls and payments of duty.

644 Which outline the employment of full-time staff experienced in setting up and managing small-business enterprises and to provide advice and assistance in the development and implementation of long-term business enterprises with Zambian majority ownership businesses that could have continued after the termination of mining operations at Bwana Mkubwa.

645 Interviews with Simon Capper, 30 October 2003 and L. M. Lishomwa, 29 October 2003.

regulations facilitated the withdrawal of three of the seven initial mining investors from Zambia and before Anglo American and Binani fulfilled most of their investment pledges (Fraser & Lungu, 2007:20).[646]

The lack of punitive measures in development agreements in case TNCs abrogated their responsibilities also enabled RAMCOZ to disregard certain obligations during receivership, such as a failure to pay its workers and creditors,[647] without recourse to significant punitive action for corporate irresponsibility. A further significant weakness is the failure of the development agreements to link the activities of TNCs to have recourse to the ultimate shareholders. Such a linkage would have imposed a significant penalty on the ultimate shareholder (the obligation of the vehicle), in the case of withdrawal.[648]

In contrast, the put option clauses that the IFC and CDC established with Anglo American protected their interests, through obligations in the shareholders agreement that obliged Anglo American to buy out the IFC and CDC for the same amount for which they bought their shares in ZCI,[649] should it depart from KCM.[650] The put option clause also enabled the IFC and CDC to pull out of KCM, together with Anglo American.[651] The protection that the put option clause provided to the IFC and CDC highlights the importance of an exit clause in protecting various participants, should mining companies depart from Zambia.

Accordingly, the easy exit that the lack of an exit clause enabled for the mining TNCs and the failure to link their activities to having recourse to the ultimate shareholders of the mining TNCs, have benefited the mining TNCs. However, these omissions had a harmful impact on the Zambian economy. Higher sunk costs, discussed below, would also have thwarted withdrawals of TNCs from Zambia.

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646 Interview with Stella Motale, 23 October 2003.
647 Which the government decided to settle (interview with David Chilipamushi, 20 October 2003).
648 Interview with Simon Capper, 30 October 2003.
649 An amount of US$25.4 million each (Africa Research Bulletin, 2002b:15349; Times of Zambia, 2002:2).
650 Interviews with Stella Motale, 23 October 2003 and Simon Capper, 30 October 2003.
651 Interview with Stuart Cruickshank, 28 October 2003.

6.5.1.7 Measures encouraging greater investment and higher sunk costs from mining TNCs in the mining sector

The dominant bargaining leverage of TNCs enabled them to, generally, set the terms of their investment obligations in the mining sector, which curtailed higher investment levels that potentially pertain to mining TNCs. In the short term, most of the mining companies failed to fully honour their investment pledges as set out in the development agreements. Lower investments of mining TNCs, in the face of the ability of mining TNCs to externalise 100% of their profit that limited higher sunk costs of TNCs, facilitated the exit of mining TNCs from Zambia.[652]

Various loopholes in government measures enabled mining TNCs to lessen or delay, in the short term, their investments in Zambia. These measures still entail, firstly, a failure of the government to hold TNCs firmly accountable for fulfilling their investment pledges that enabled TNCs to delay or to abrogate their investment obligations, as noted in Section 6.1.2. Secondly, the clause in the agreement of mining companies entitling some mining TNCs to a proportional reduction of their capital expenditure commitment for the first three years and to close or significantly curtail operations temporarily or permanently,[653] also limited higher investments. Such restrictions are subject to the commercial viability of their operations, determined at the discretion of TNCs.

Thirdly, the sanctioning of deferred cash payments to mining companies that was against a clause in the Privatisation Act, stipulating that these terms be made available only to Zambian nationals and MBOs and only for the purchase of shares, also hinders greater investments in Zambia. These concessions would have an unfavourable impact on Zambia if mining TNCs exit before paying their deferred cash obligations. This was the case with Anglo American that was able to depart from Zambia before paying the rest of the US$60 million for the mines it had acquired (ZPA, 2003:2).[654] Fourthly, the non-recourse nature of investments by TNCs in Zambia precludes the government from demanding compensation from shareholders of TNCs, should these companies fail to

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652 Interviews with John Kangwa, 21 November 2003 and Honourable Captain Moono, 2 December 2003.
653 For reasons such as certain force major events, or, adverse economic circumstances.
654 Interview with L. M. Lishomwa, 29 October 2003.

fulfil their commitments.

The poor enforcement of their investment obligations has advantaged the mining TNCs. It has had however, a negative influence on the Zambian economy. A stipulation in the bid process for secured investments well ahead of the allocation of bids, rather than pledged investments, which also limited greater public finances from the privatisation of the mines, would have ensured higher investments from mining TNCs in the host country (Pennings, 2008:489). Moreover, the imposition of higher sunk costs that would extend the timeframe before investors get their return on investment, making it more costly for foreign investors to pull out of Zambia, would in the short run have acted as a disincentive for TNCs to depart from the host country. The capacity of TNCs to extract concessions from the host country would also decline once they had sunk their own input into the host country.

Higher sunk costs of TNCs, through significant investments into Zambia, would further improve the bargaining leverage of the Zambian government for making greater demands on the mining TNCs. This is because the bargaining strength of a host country is weakest during the periods before foreign firms have sunk inputs into the country (Heilleiner, 1989:1463). A stronger capacity of the state and its institutions would also have enabled the government greater leverage to ensure that mining TNCs respect their investment commitments.

6.5.1.8 Measures to control instability in the foreign currency reserves and the exchange rate

Section 5.4.2 of Chapter 5 and Section 6.2.3 above show that under TNCs' ownership of the mines the TNCs also utilised their ability to influence the exchange rate to promote their *x*-efficiency objectives and to elicit favourable terms during negotiations with the government. Weaknesses in government policies abetted the high externalisation of foreign currency and money laundering.[655] In particular, the liberal policies that the IMF and World Bank imposed on the government enabling mining

[655] Interviews with Fred M'muembe, 14 October 2003 and Reibner Hoffner, 15 October 2003.

companies to repatriate 100% of their profit from copper sales[656] and policies allowing companies to retain a large portion of foreign currency from mining in offshore corporate accounts continue to facilitate these practices (Africa Research Bulletin, 2001c:14687; Van Buren, 2003:1151). These policies preclude government intervention in the foreign exchange market,[657] necessary to safeguard against sudden outflows of foreign exchange.

However, policies that the Central Bank and the Commerce, Trade and Industry Ministry recently introduced to stop goods (including equipment) and services from being quoted in foreign currencies, to prevent the US dollar from undermining the Zambian kwacha as the local tender in Zambia, has created greater stability in the exchange rate (Bank of Zambia, cited in Africa Research Bulletin, 2003c:15633). Some restrictions on the repatriation of mining surpluses would also have created greater stability in Zambia's foreign currency reserves. Laws compelling foreign companies to retain some of their foreign exchange earnings from mining in Zambia, also through deposits with the BoZ for conversion into the local currency,[658] would have curbed significant depreciations and fluctuations in the value of the kwacha (US & Commercial Service and US Department of State, 2005:19; ZDA, 2009:8; Bank of Zambia,[659] 2010).[660] However, despite the Zambian Finance Ministry announcing in 2003 to limit repatriation activities, partly through introducing laws requiring that 75% of export proceeds be banked locally, these policies were still not introduced by 2010.

In contrast to the liberal policies of the Chiluba government, certain policies of the Kaunda government led to good control and accountability over Zambia's foreign exchange.[661] These encompassed the depositing of all mining sales revenue with the

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[656] Which encourage private companies to retain most of the foreign exchange obtained from copper sold at the London Stock Exchange in external accounts in the short run.

[657] Such as laws forcing the mining companies to reinvest a portion of their profit from mining activities into Zambia.

[658] Under government ownership, most revenue from mining was deposited with the Reserve Bank.

[659] Confirmed by e-mail on 17 May 2010 from: Dinde Simacheche, SDINDE@boz.zm, Bank of Zambia, in response to questions by author.

[660] Interviews with Danny Kalyalya, 31 October 2003; David Chilipamushi, 20 October 2003 and John Lungu, 12 November 2003.

[661] However, despite efforts to improve export earnings in the late 1980s the supply of foreign exchange remained inadequate to meet imports, exports and external debt service requirements (Africa Now, 1987:31).

BoZ[662] and a requirement that mining executives apply to the BoZ for foreign exchange.[663] In the late 1960s, the Kaunda government also placed restrictions on the amount of capital that companies could repatriate out of Zambia (and only in the form of dividends and royalties). However, severe limitations on the amount of foreign exchange that local companies were able to access, which significantly restricted the foreign supplies that local companies could buy, stifled their development.[664]

Accordingly, the foreign exchange regime that the IMF and the World Bank imposed on the MMD government, to promote their neo-liberal policies, was highly beneficial to mining TNCs. Conversely, in the short-term these policies as well as government policies enabling mining TNCs to repatriate all their profit had a destabilising impact on both the exchange rate and on the level of foreign currency reserves of Zambia from mining, under the ownership of TNCs. Effective state intervention is necessary to enable the retention of higher foreign currency reserves from mining in the Zambian economy and to safeguard against sudden outflows of foreign exchange under TNCs' ownership of the mines.

6.5.2 The monitoring and enforcement capacity of the government in controlling the activities of private mining TNCs

Weaknesses in the monitoring and enforcement capacity of the government in controlling the activities of mining TNCs hinder effective control of the government over the activities of the TNCs and of the follow-up of the post-privatisation process, enabling the mining TNCs to frequently abrogate their responsibilities.[665] The weak monitoring and enforcement capacities and the legal loopholes represent major limitations of the privatisation process, the post-privatisation monitoring process and of the operations of TNCs in Zambia.[666] Some academics consider these limitations amongst the greatest weaknesses that Zambia had experienced, by 2003 under private

662 Unlike at present where sales revenue is deposited into company accounts.
663 With supporting documentation as to how these were to be used (interview with Francis Kaunda, 20 October 2003).
664 Interview with Eddy Kapungulya, 13 November 2003.
665 Interviews with Ladslous Mwansa, 7 October 2003; David Chilipamushi, 20 October 2003; Dennis Wood, 21 October 2003; Andygean Luombe, 8 October 2003 and Bernadette Mwakacheya, 17 October 2003.
666 Interviews with Ladslous Mwansa, 7 October 2003 and Alick Lungu, 14 October 2003.

ownership of the mines by TNCs.[667]

Proactive and transparent monitoring of results is important to analyse the impact of policies and to introduce remedial action that would facilitate the enforcement of binding agreements. It is also important, together with the enforcement of laws, for curbing corruption (World Bank, 2002b:31; Rose Ackerman, 1997:48). The main factors accounting for the weaknesses in the monitoring and enforcement capacity of the Chiluba government in controlling the activities of the mining TNCs are the poor bargaining leverage of the government over the mining TNCs, the poor capacity of government institutions, the untransparent nature of the development agreements and the slow court system. These are briefly considered below.

Firstly, the significant power of mining TNCs over the weakened and poorly resourced government enabled these TNCs to often abrogate their obligations. Politicians, apprehensive that investors might withdraw from their countries, tended to accommodate these practices (ZCCM-IH, 2001:1).[668] The lack of voting rights of the directors of the ZCCM-IH, representing the government in the private mining companies, except for issues that are of critical importance,[669] has also weakened the leverage of the government in its relation with mining TNCs.

Secondly, the poor capacity of institutions tasked with monitoring the operations of mining companies, in accordance with the development agreements,[670] in particular the Ministry of Mines and Mineral Development and the ZCCM-IH, also reduced more effective monitoring and implementation of laws regulating the activities of TNCs.[671] Inadequate resources (also of manpower),[672] poor access to information and the absence of longer-term development plans for the country have largely accounted for the poor

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[667] Interviews with David Chilipamushi, 20 October 2003 and Danny Kalyalya, 31 October 2003.
[668] Interviews with Bernadette Mwakacheya, 17 October 2003; Thomas Kabandama, 13 November 2003; Fred M'muembe, 14 October 2003 and David Chilipamushi, 20 October 2003.
[669] In which case the golden share the government enjoys in the mining company would enable it to influence decisions.
[670] Interview with Wilphred Katoto, 12 November 2003.
[671] Interviews with Danny Kalyalya, 31 October 2003; Fortune Kamusaki, 25 November 2003; David Chilipamushi, 20 October 2003; Mark O' Donnell, 16 October 2003; Alick Lungu, 14 October 2003 and M. Shandavu, 10 October 2003.
[672] As many of the skilled technocrats departed for the private sector.

capacity of these institutions.[673] The brevity of many of the ministerial terms[674] further undermined the capacity of the Ministry of Mines and Mineral Development to monitor the activities of mining TNCs.[675] These weaknesses also prevented more effective implementation of government mining policies (The Economist Intelligence Unit, 2002:8).[676] Moreover, the erosion of the power of mining trade unions and the anti-union bias of TNCs diminished their capacity to enforce the protection of the Zambian mineworkers against certain operations of mining TNCs.

Poor access to information regarding certain mining activities further degrades the capacity of the Ministry of Mines and Mineral Development to monitor the activities of mining TNCs. In particular, the disbandonment of the Mineral Marketing Corporation (MIMACO) that collected various information on mining in Zambia, during Kaunda's rule, and the subsequent decentralisation of information of different activities of the mining sector contributed considerably to the inaccessibility of metal sales figures.[677] Moreover, subsequent to the disbandonment of MINDECO that was in charge of mineral development during the Kaunda government, the absence of good annual reports of mining TNCs and their inaccessibility to the public under private ownership of the mines, make it difficult to monitor mining sector activities in Zambia.[678] The annual reports of mining TNCs, submitted to the Mines Safety Department, the Ministry of Mines, the ZRA, the BoZ and the ECZ, often lack clear data on the contributions of each of the mining firms to national tax that prove difficult to obtain (Fraser & Lungu, 2007:17).

The elimination of long-term development plans during Chiluba's rule, with the dissolving of the Ministry of National Planning and associated institutions such as the NCDP, further lowers the capacity of the government to effectively monitor and implement laws, also those governing the mining TNCs.[679] The NCDP was involved in

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673 Interviews with Bernadette Mwakacheya, 17 October 2003; David Chilipamushi, 20 October 2003; Reibner Hoffner, 15 October 2003; Willie Sweta, 30 October 2003; Fred M'muembe, 14 October 2003 and Dindiwe, 11 December 2001.
674 Which makes it difficult for ministers to master their briefs.
675 No monitoring was done in 2001 (interview with Dindiwe, 11 December 2001).
676 Interview with Zion Simwanza, 1 December 2003.
677 Such as information on the receipt of money to the BoZ, which was easily available before.
678 Interview with Zion Simwanza, 1 December 2003.
679 Interviews with John Lungu, 12 November 2003; Alick Lungu, 14 October 2003 and Valentine Chitalu, 22 October 2003.

planning, monitoring and evaluation, and set five-year development plans during Kaunda's government. The absence of national development plans, without itemised accounts of government spending, which made the retracing of government spending difficult, also obstructed enforcement and facilitated corruption in the mining sector under the Chiluba government. The abolishment of long-term development plans also led to the uncoordinated functioning of many state bodies (Committee on Economic Affairs and Labour, 2001:110). Chang (1994:13) considers long-term development plans as necessary to assist the 'entrepreneurial vision' of the state.

The replacement of the national policies by shorter-term IMF and World Bank austerity programmes during Chiluba's rule, further weakened the power of economic bureaucracies and of other institutions to adequately implement government policies[680] and their ability to attain embedded autonomy. Powerful economic bureaucracies, an important ingredient in the development of developmental states, that organise the interaction between the state and the economy for strategic economic direction and co-ordination, possess effective power and high technical competence. These institutions also enjoy relative autonomy or insulation for developing economic policies (Leftwich, 1995:425). The National Economic Advisory Council that the MMD government established in an advisory role proved to be weak.[681] The reintroduction of longer-term development plans in 2006, during Mwanawasa's government, culminating in the establishment of the country's FNDP,[682] points to some extent to an admission that the abolishment of the national development plans in Zambia during Chiluba's government was a mistaken policy (The Economist Intelligence Unit, 2008a:4).[683]

Thirdly, the confidential nature of development agreements[684] precludes access to their contents obstructing better monitoring and enforcement of investor compliance of these agreements.[685] The public, trade unions and even the regulating authorities mandated to

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[680] Interviews with Chansa Chifumbe Winston, 15 December 2001; David Chilipamushi, 17 December 2001; Danny Kalyalya, 14 December 2001 and Alick Lungu, 20 December, 2001.
[681] Interview with John Lungu, 12 November 2003.
[682] The FNDP sets out, in detail, the plans for reform and direct the economic development of Zambia.
[683] Interview with Valentine Chitalu, 22 October 2003.
[684] Interview with Charles Muchimba, 18 November 2003.
[685] Interviews with Charles Muchimba, 18 November 2003; John Kangwa, 21 November 2003 and Agnes Bwalya, 9 November 2003.

ensure that the private mining companies fulfil commitments specified in the development agreements do not have easy access to these agreements. The untransparent nature of the development agreements left certain obligations, specified in the development agreements, unfulfilled (Committee of Economic Affairs and Labour, 2000:38).[686] However, the development agreements of J and W Holdings (that acquired ownership of the mines more recently) were more transparent and involved the active participation of the mining trade unions as well.[687] Fourthly, difficulties in obtaining a swift conviction, largely due to the slow court system,[688] also rendered enforcement difficult.[689] The recent establishment of the Commercial Court and Arbitrators, obliging the Chief Justice to appoint a tribunal when a complaint is lodged, is nevertheless likely to speed up the long delays in the legal process in commercial disputes.[690]

From the above discussion, it is noted that despite the existence of various laws to address malpractices of mining TNCs,[691] the Zambian government possesses a poor monitoring and enforcement capacity in controlling and directing the activities of private mining TNCs to ensure greater developmental and equitable outcomes for Zambia. An adequate, coherent post-privatisation monitoring unit is necessary to enable the new mining investors to respect their obligations (Committee of Economic Affairs and Labour, 2000:52, 72). Certain weaknesses in the regulations, institutions and in the monitoring and implementation of laws governing the activities of mining TNCs, that also limit the retribution capacities of the government in the event of malpractices or withdrawal,[692] favoured mainly the mining TNCs with severe negative repercussions for Zambia. Institutional weaknesses in the public sector,[693] as well as shortcomings in the private sector, constrained the government's ability to address more effectively the problems that arose under private ownership of the mines (Burnell, 1995:677-678).[694]

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[686] Interview with Willie Sweta, 30 October 2003.
[687] Interviews with Charles Muchimba, 18 November 2003 and John Kangwa, 21 November 2003.
[688] Interviews with Silane Mwenechanya, 24 October 2003; Honourable Captain Moono, 2 December 2003 and Andygean Luombe, 8 October 2003.
[689] For instance, it is unlikely that Chiluba, who faces 169 counts against him, will be convicted in his lifetime, given that each count takes several years to be addressed (interview with Honourable Captain Moono, 2 December 2003).
[690] Interview with Danny Kalyalya, 31 October 2003.
[691] Interview with Bernadette Mwakacheya, 17 October 2003.
[692] Interviews with John Kangwa, 21 November 2003 and Alick Lungu, 14 October 2003.
[693] Interview with Danny Kalyalya, 14 December 2001.
[694] Interview with John Kangwa, 21 November 2003.

These weaknesses, owing mainly to the poor bargaining position and capacity of the Zambian government, have in particular eroded benefits to the mineworkers and the suppliers of the mines. This is contrary to the strong corporatist roles that governments of developmental states enjoy in guiding the activities of TNCs towards more favourable outcomes for their countries. A stronger state capacity that would have enabled the government to play a greater corporatist role in directing the activities of the TNCs and to act more independently of donors seems necessary for more advantageous outcomes for the host country from the participation of mining TNCs in the Zambian economy (Leftwich, 1995).

6.5.3 Political-economic implications of the activities of TNCs in the mining sector

The impact of the activities of the mining TNCs on different stakeholders of Zambia, namely the mining TNCs, the Zambian suppliers, the mineworkers and the mining community and on the Zambian economy are examined below.

The influence on mining TNCs

The dominant leverage of mining TNCs over the Zambian government enabled them to influence the government into adopting policies that promoted their interests. This resulted in a shift of a major portion of the rent element from mining in favour of mining TNCs. The mining TNCs continue to be advantaged especially through the concessions that they have negotiated with the government. In particular, KCM and MCM and more recently J and W benefited the most from the additional concessions that they still enjoy over mining companies that privatised earlier. Moreover, foreign investor-friendly policies pushed by the IMF and the World Bank that the country's high dependence on aid forced it to adopt were also greatly beneficial to foreign investors. The inclination of the TNCs to invest a large proportion of profits as dividends rather than allocate them for reinvestment into the mining sector, as well as the non-recourse nature of the activities of TNCs in Zambia, also favoured predominantly foreign shareholders of the mining TNCs.

It is further noted from the above discussion that certain weaknesses in government capacities mainly of their institutions, laws and policies regulating the activities of mining TNCs and in their implementation also proved beneficial to the mining TNCs. This is partly due to these weaknesses making it difficult to hold the TNCs accountable should they abrogate their responsibilities. While the limitations in government laws and institutions shifted gains in favour of mining TNCs, these had a highly negative impact on the Zambian economy.

The weaknesses in laws and policies that continue to favour the mining TNCs include:

- excessive foreign investor-friendly government policies (also through incentives and concessions) that limit government tax revenue from mining TNCs;
- lack of exit clauses in development agreements limiting recourse to punitive action in the event of TNCs' exiting from Zambia. The lack of exit clauses may have a devastating effect on the Zambian economy if the mining TNCs do withdraw from the country;
- loopholes that curtail higher investments and sunk costs from mining TNCs in Zambia;
- liberal policies in exchange controls that enable mining TNCs to repatriate all their profits out of Zambia and facilitate transfer pricing practices of mining TNCs;
- the choice of bilateral agreements for regulating the mining TNCs over the Safes Agreement (that would have promoted the interests of Zambians). Within a weak state these bilateral agreements adversely influenced the interests of the mineworkers, the mining community and the Zambian economy;
- poor monitoring and enforcement of legislation; and
- the limited shares that the government retained in the mines, which reduce returns for the government from improved performance of the mining sector that instead accrues mainly to the mining TNCs.

<u>Impact on suppliers</u>

The preference of mining TNCs for replacing local suppliers with foreign suppliers, possibly also from their own subsidiaries, to meet their *x*-efficiency and profit-maximising objectives enabled the foreign backward-linked companies to the mining sector greater entry into the Zambian market. However, the practices of TNCs to displace local capital with foreign suppliers disadvantaged the local suppliers. This corresponds with the argument of dependency theorists that TNCs contribute to a highly unequal income distribution in host countries, with negative redistributive implications that may deflect the host country's development from a more desired path (Helleiner, 1989:1454).

Various shortcomings in government regulations and policies and enforcement measures, elaborated upon in Section 6.5.1, also limited greater gains for local suppliers from the activities of mining TNCs. Most notably, the government failed to protect local suppliers against practices of mining TNCs that influenced them adversely. Bilateral development agreements between the government and mining TNCs, entitling the TNCs to select their own suppliers, also typically favoured foreign suppliers.

Moreover, the continued lack of effective industrial policies for promoting local capacities, which were crucial to the progress of developmental states further disadvantaged local suppliers. Rather, as discussed in Section 4.2.2.1 of Chapter 4, foreign investor-friendly government policies from which local suppliers were excluded, liberal policies and the higher costs of production that certain policies of the Chiluba government imposed on local suppliers[695] lowered benefits to the local suppliers. These policies further assisted foreign companies to gain increasing entry into the market of backward-linked industries and suppliers to Zambia's mining sector. Accordingly, the highly liberal foreign investor-friendly policies represent the antithesis of an effective industrial policy necessary to promote the development of local industries. The failure to establish industrial policies encouraging greater vertical and horizontal linkages between local suppliers and mining TNCs also deprived Zambia of significant benefits that such linkages hold for the local suppliers.

[695] The policies that increase the cost of local production include the high interest rates and the depreciation of the kwacha, which respectively accompanied the auctioning of the financial market and the exchange rate, as well as the higher taxes and duties placed on local businesses over foreign businesses. These policies increased especially the price of imported mining inputs.

Impact on the mineworkers and mining communities

A major shift occurred in the political economy of the mineworkers and of the mining community under private ownership of the mines by TNCs. The stronger bargaining leverage of TNCs, enabling them to demand the retrenchment of many mineworkers during the bidding process reduced the redistribution of benefits to the mineworkers. It likewise diminished the power of the government to demand better conditions of employment for workers. In contrast, under Kaunda's government, the mining policies were highly favourable to the mineworkers and the mining community, discussed in Section 4.3.2.3 of Chapter 4.

Additionally, as is noted in Section 5.4.2 of Chapter 5, certain *x*-efficiency objectives under the TNCs' majority ownership of the mines encouraging the mining TNCs to lower conditions of employment affected the mineworkers adversely. It is noted that conditions of employment were lowered through high reductions in the number of permanent mineworkers and an increasing shift of permanent workers to contract employment and casual employment. The refusal of the mining TNCs to assume responsibility for non-core mining facilities had a further unfavourable influence on the welfare of the mining community. The substitution of local managers with expatriate managers in several mining companies also favoured expatriates over local managers.

Furthermore, several loopholes in government institutions and in their regulatory and enforcement capacity, noted in Section 6.5.1 enabled the TNCs to pursue less worker-friendly policies than was the case under Kaunda's government. Briefly, these loopholes continue to entail the weak implementation of labour laws, a reduction of the power of mining trade unions, insufficient obligations placed on mining TNCs to train Zambian mineworkers and to allow for a greater participation of Zambians in the management structures of TNCs. The absence of policies encouraging horizontal linkages between local capacities and mining TNCs that would have enabled the transfer of greater know-how from TNCs to the host country further deprives Zambia of the significant development of its human capital that such linkages with mining TNCs hold for the host country. The weak enforcement of the legislation was mainly because of the poor bargaining power of the government and because of the capacity constraints of the institutions governing the protection of workers.

Influences on the Zambian economy

Within a weak state the government lacked the leverage to ensure a greater capturing of returns from mining and to direct the activities of mining TNCs to more favourable outcomes for Zambians under private ownership of the mines by TNCs. Rather, as noted above, the shift in the returns from the exploitation of the copper mines under private TNCs' ownership of the mines mainly in favour of the mining TNCs, caused a poor redistribution of mining surpluses to the Zambian economy. This was also the case during the copper price boom when the mining companies enjoyed high profits. The shift in returns had a highly negative impact on the economic development of Zambia. Moreover, certain activities of some mining TNCs, in particular those of Binani at RAMCOZ, together with the government's acceptance of the liabilities of the company and its assumption of the role of the receiver of RAMCOZ constituted a great drain of Zambia's resources.

The factors that for the most part continue to account for the weak transfer of benefits to the national economy under TNCs' ownership of the mines are:

- The significant reduction in government tax from mining mainly because of the high concessions granted to mining companies. Instead, the tax burden is shifted to the local population in the form of the high VAT and electricity rates imposed on the local population and through the higher PAYE tax rate.
- The repatriation of mining profits and resources out of Zambia (also likely through transfer pricing practices and as dividends to the foreign shareholders of mining TNCs).
- The ability of mining TNCs to manipulate the foreign currency reserves of Zambia and the value of the kwacha contributing considerably towards the volatility in both Zambia's foreign currency levels and in the exchange rate of the kwacha, jeopardising the economic security of the country.

- The absence of a stabilisation fund, established from mining surpluses. Such a fund would have diminished the negative impact of fluctuations in copper prices on the government revenue from mining.
- Several of the profit-maximisation pursuits of the mining TNCs, often aimed at fulfilling the global interests of the parent company that might clash with the interests of the host country, such as the departure of Anglo American from Zambia.

Nonetheless, the mining TNCs contributed significantly towards much needed capital and technology investment in the mining sector, in comparison to what was the case in the late 1990s. However, their failure to fulfil several of their investment commitments also detracted from this benefit.[696]

The poor redistribution of resources, under private ownership of the mines, represents a classic example of a predominantly mining-dependent economy, suffering from the 'Dutch disease'. The 'curse' of a resource-rich economy that the Zambian economy also experienced under government ownership, especially in the context of low copper prices and Zambia's high economic debt, was considerably amplified under private TNCs' ownership of the mines. This is mirrored in the increases in poverty levels under private ownership of the mines largely as a result of the high repatriation of profits. The repatriation of profit together with concessions reduced Zambia's foreign currency reserves and savings from mining. However, the 'curse' needs not be inevitable.

Sections 6.5.1 and 6.5.2 and the above discussion show that various loopholes within government institutions and laws regulating the activities of mining TNCs in Zambia and the poor monitoring and enforcement mechanisms of the government to curb regulatory diversions of TNCs also limited greater gains for Zambia from the mining TNCs. A strong capacity of the state in mining, which the Zambian government has failed to establish, is crucial to maximise rent from mining and to limit opportunistic operations and negative outcomes of the participation of mining TNCs in the economy.

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[696] These loopholes entail a failure of government measures to hold TNCs firmly accountable for fulfilling their investment commitments, policies entitling mining TNCs to a proportional reduction in the short term of their capital expenditure commitment and to close or significantly curtail operations, temporarily or permanently at their discretion, subject to the viability of their operations and the sanctioning of deferred cash payments from the sales of the mines.

It is also necessary to define and direct the activities of mining TNCs towards more favourable outcomes for Zambia. Moreover, under a strong state capacity, as is the case with Botswana, the country is likely to escape the 'curse' of a minerals-based economy (Iimi, 2006:1).

In the mining sector, a stronger state capacity requires high institutional capacities, deemed also important to reverse the 'paradox of plenty' in resource-abundant countries (Action Aid International *et al*., 2009:x; Bebbington *et al*., 2008:10). Additionally, industrial policies which promote the nurturing of local capacities, through tariffs, quotas and through a degree of good government discipline that would have enabled it to make greater demands on TNCs, are essential to increase state capacity. A greater corporatist role of the state over TNCs represents a further important element to augment the capacity of the state to direct the activities of TNCs towards higher gains for the Zambian economy.

In summary, under the TNCs' ownership of the mines, within a weak state in which mining TNCs dominated the negotiations over investments and over the returns from copper mining, and alongside liberal and excessive foreign-investor friendly policies, the political-economic landscape of Zambia was fundamentally altered. The poor returns and redistribution of surpluses from the extraction of minerals shifted benefits to the mining TNCs, their shareholders, and the foreign suppliers of mining inputs in Zambia. Expatriate managers are also favoured over local managers in several of the mining companies. These policies have marginalised the local mineworkers and suppliers to the mines and affected the Zambian economy adversely.

The advantages to the national economy from the participation of mining TNCs in Zambia were severely limited and were mainly in the sphere of technological and capital inputs that the TNCs invested in the mining sector. Even then, these benefits were lowered, in the short term, as the technological and capital inputs from mining TNCs were less than they had pledged. Instead of promoting Zambia's development some of the activities of mining TNCs, in fact, amounted to a draining of the resources of Zambia that promoted underdevelopment. These outcomes correspond closely with the arguments of Global Reach theorists and of neo-imperialists that TNCs' activities drain the resources of developing host countries.

Broadly, the various costs to the Zambian economy associated with the activities of mining TNCs in Zambia included:

- significant decreases in government revenue and in foreign exchange from mining mainly owing to the high concessions granted to the mining TNCs;
- the repatriation of mining profits out of the country;
- the degrading of the conditions of employment of mineworkers; and
- the undermining and substitution of local capacities largely as a result of practices of TNCs to replace them with foreign capacities.

However, the weak government capacities, rather than the activities of TNCs per se greatly contributed to the 'resource curse'. The poor returns to the Zambian economy from the participation of TNCs in the mining sector were also largely the result of the limited bargaining leverage of the government and shortcomings in laws and institutions and in their enforcement to steer the activities of TNCs towards greater returns for Zambia. These enabled the mining TNCs to behave opportunistically. A higher capturing of rent and investments also into alternative non-exhaustible sectors would have increased the sustainability of the economy and the economic diversity of Zambia and diminished the effects of the 'Dutch disease' from which the Zambian economy is suffering. A higher state capacity, largely achieved through competent institutions, industrial policies to also promote a stronger economic development of the country and a greater corporatist role of the government, would have ensured more successful outcomes from the activities of mining TNCs in Zambia.

CHAPTER 7

7. SUMMARY, RECOMMENDATIONS AND CONCLUSION

The study sought to assess: the impact of different policies of the Kaunda and Chiluba governments on the mining sector; the privatisation of the mining sector and the impact of changing ownership and management structure and objectives of Zambia's copper mines on the economy; and the roles of TNCs in the mining sector of Zambia. The socio-economic and political-economic consequences of the activities of TNCs and of the government are important subsets of this examination.

This chapter presents a summary of the findings and postulates recommendations for more beneficial privatisation and private ownership of the mining sector, as well as for greater advantages for Zambia from the activities of mining TNCs. This is followed by concluding remarks of the study.

7.1 THE IMPACT OF DIFFERENT POLICIES OF THE KAUNDA AND CHILUBA GOVERNMENTS ON THE MINING SECTOR

The different policies that the Kaunda and the Chiluba governments adopted for the mining sector influenced the development of Zambia's mining sector in distinct ways. The IMF and World Bank policies that were intermittently introduced during Kaunda's government from 1983-91 and fully adopted from 1992 under Chiluba's government further impacted on the mining sector.

7.1.1 Economic outcomes of the policies of the Kaunda government

The accrual of surpluses from the returns of copper mining mostly to the TNCs that enjoyed full ownership of the mines, and their practices of investing a large proportion of mining profits as dividends, significantly motivated the nationalisation of the mines in 1969. The transfer of considerable profits as dividends resulted in gross undercapitalisation of the mines and excessive borrowing after independence. However, government policies granting the mining TNCs preferential treatment in foreign exchange control regulations also aided the externalisation of mining surpluses during private management of the mines. The preferential treatment included permitting the mining TNCs to automatically externalise non-taxable profits, dividends, management fees and income from the sales of the private mining companies. Poor application of the Zambianisation policies[697] by the TNCs and their transfer pricing policies and practices to externalise profits precipitated the Kaunda government's revoking of the management contracts of mining TNCs in 1974 under government ownership of the mines.

Contrary to private ownership, during the majority government ownership and management of the mines the electoral-maximising motives of the Kaunda government favoured a redistribution of a considerable proportion of mining revenue to other areas of the economy. The redistributive measures, together with industrial policies that the Kaunda administration adopted, enabled a significant period of development in the 1960s and 1970s for the Zambian economy. These policies precipitated the notable development, especially of social services and the human capital of local Zambians. Zambianisation policies proved particularly instrumental in developing the human capital of Zambians.

The redistributive policies were highly effective in redressing the significantly uneven distribution of income and wealth that adversely influenced local Zambians during Federal rule. However, adequate reallocation of revenue from mining was only possible when mining surpluses were readily available. Void of effective recapitalisation of the mines and growth, the reallocation of mining surpluses into unproductive sectors undermined the sustainability of the redistributive capacity of the government.

The industrial policies of the Kaunda government, nurtured mainly through ISI policies introduced between 1965 and 1980, and the development of the parastatal sector largely from revenue from mining, contributed to the rapid development of the manufacturing sector, mainly during the first decade of Kaunda's rule. Manufacturing was almost non-existent at independence (in 1964). The development of the manufacturing sector promoted greater diversification of the economy than was the case during the pre-

[697] Entailing greater Zambian participation in the economy at higher employment levels and in managerial positions of companies.

independence period. However, the poor integration of the mining sector with the local manufacturing sector, and the high import content of locally based backward-linked industries to the mining sector[698] reduced the impetus of the mining sector as an engine of growth for other sectors.

Furthermore, without the setting of strict targets that local industries had to meet, to encourage infant industries[699] to 'grow up' and become internationally competitive, the protectionist policies (extended mainly to the parastatal-dominated manufacturing sector) encouraged inefficiencies in these firms. The extension of protectionist policies mainly to the parastatal sectors also disadvantaged private sector businesses. The emergence of several inefficient industries or 'lame ducks' that remained highly dependent on subsidies under the protectionist policies of the Kaunda government obstructed sustainable growth in the manufacturing sector. As a result, the lifting of controls and the full-scale introduction of trade liberalisation policies in the 1990s under Chiluba's government culminated in the bankruptcies of many local support industries to the mining sector. Protectionist policies are therefore a necessary but insufficient condition for promoting the development of competitive local industries.

7.1.2 The impact of the policies of the Chiluba government on the development of the mining sector

The pervading influences of the SAPs and liberal policies promoted by the IMF and the World Bank on mining and on other policies of the Chiluba government significantly diminished the government's role in setting its own industrial policies in the mining sector. The SAPs, in particular demand management and supply measures, had a similar but more severe adverse impact respectively on workers and local suppliers under Chiluba's government than during Kaunda's government. This was reinforced by the MMD government adopting these policies more rigorously.

Although a lowering of government expenditure required by the demand management

[698] Or industries that supply the mines with inputs.

[699] New industries in their early stages of development, and in need of protection from predatory competition through tariff and non-tariff barriers until they become established (Businessdictionary.com, 2010).

programmes of the SAPs was necessary to reduce the high government deficit, the decline in government investments in productive sectors affected the mining sector and the Zambian economy unfavourably. Moreover, while reductions to the excess labour force in the mining sector subsumed in demand management measures were necessary, a failure to create alternative employment to absorb those that became unemployed contributed to the high unemployment levels of mineworkers in Zambia. Mining employment declined from 62 100 in 1992 immediately prior to the Chiluba government coming into power to 47 700 in 1996 before the mines were privatised. Furthermore, the lower spending on social services caused a deterioration of social services to the mining community.

Supply-side measures, in particular the higher interest rates that accompanied their decontrol and the negative impact of high inflation as a result of the hike in the costs of mining inputs on local suppliers, adversely affected the local support industries linked to the mining industry. The high import content for intermediate inputs of local manufacturers overrode the benefits that a lower exchange rate, following the depreciation of the kwacha, generally hold for reducing local costs and for encouraging a switch to the local procurement of mining inputs. On the contrary, the crash in the value of the kwacha against the currencies of Zambia's major trade partners caused a large rise in inflation, and subsequently resulted in a macro-economic meltdown that compounded Zambia's debt problems. Greater inter- and intra-industry linkages of Zambia's industries that would have reduced their dependence on imports for intermediates before liberalisation policies were introduced, would have ensured a more beneficial impact on locally-based suppliers from the depreciation of the local currency.

Moreover, in the context of the weak local industries and the highly imperfect markets, aggressive foreign competition encouraged by free trade policies caused the bankruptcy and relocation of many locally-based industries and suppliers, including those linked to the mines. Especially more competitive South African suppliers that entered the Zambian market following the introduction of free trade policies replaced several locally-based backward-linked industries in the supply of mining inputs. These consequences of free trade policies contrast with those of protectionist policies that the Kaunda government introduced that favoured local suppliers. Other foreign investor-friendly policies that the Chiluba government adopted also had a detrimental impact on the local backward linkages to the mining sector. Summaries of the impact of the privatisation policies and the private ownership of the mines by mining TNCs during Chiluba's government are respectively considered in Section 7.2 and 7.3 below.

7.2 THE PRIVATISATION OF THE MINES AND THE IMPACT OF THEIR CHANGING OWNERSHIP AND MANAGEMENT STRUCTURE ON THE ECONOMY

Various interest groups influenced the privatisation decisions of the mines. In particular, the World Bank and the IMF possessed significant command in influencing the decision to privatise the mines that the government was obliged to adopt because of its weakened bargaining position, mainly due to its huge debts. Furthermore, Anglo American acquired strong control in influencing recommendations for the structure of the privatisation of the mines. Despite the poor leverage of the government in the decisions on the privatising of the mines, political interference strongly marked the privatisation of the ZCCM.

The privatisation of the mines faced major challenges that had negative consequences for the Zambian economy. Moreover, changing management objectives and structures under different ownership had dissimilar outcomes on mining performance and on the socio-economic development of Zambia. The privatisation and the private ownership of the mines also influenced the political economy of Zambia in distinct ways. 'Privatisation' refers to the processes involved in transferring ownership of the SOEs from the public to the private sector and therefore precedes private ownership. Private ownership refers to the enterprise under the ownership of the private sector.

7.2.1 Challenges limiting positive outcomes for Zambia during the privatisation of the mines

Weaknesses in the legal and institutional framework in the privatisation process, and a failure of privatisation to improve the public finances, significantly limited more advantageous outcomes from the privatisation of the mines.

7.2.1.1 Weaknesses in the legal and institutional framework in the privatisation of the ZCCM

The institutional and policy changes that the Chiluba government introduced, which undermined the institutional capacities of those bodies established to execute the privatisation of SOEs of Zambia, were contrary to prerequisites needed for more successful privatisation of SOEs. The changes that the Chiluba government introduced entailed: (i) the introduction of political interests into the privatisation process; (ii) irregularities and non-transparency in the ways in which the proceeds from the sales of the ZCCM were managed; and (iii) insufficient protection of mineworkers. Poor enforcement measures to promote more successful privatisation also limited the success of the privatisation of the ZCCM.

In the absence of effective checks and balances, increases in the discretionary power of the Chiluba government in the privatisation of the mining sector compromised the independent functioning of the ZPA (the body established to privatise all SOEs) in the privatisation of these assets. It also facilitated the alleged corruption by senior government officials during the privatisation of the mines. Non-transparent ways in which the proceeds from the sales of the ZCCM were managed further abetted corrupt practices.

The primary weaknesses in the protection of mineworkers during the privatisation of the mines included the failure of the government to create alternative employment before the mines were privatised to absorb workers left unemployed as a result of privatisation and under private ownership of the mines. The government also neglected to introduce effective social safety nets to protect workers against adverse consequences arising from the privatisation of the mines. The establishment of robust institutional and legal prerequisites, adequate social safety nets and alternative employment to absorb those left unemployed as a result of the privatisation were necessary before privatisation policies were introduced for ensuring more favourable outcomes for countries from privatisation policies (Stiglitz, 1998:19, 20; 2002:182).

7.2.1.2 Failure to improve public finances

Contrary to the neo-classical argument that the privatisation of SOEs and the private ownership of enterprises would improve public finances, the privatisation of the ZCCM failed to achieve increases in public finances through higher government revenue from the sales of the mines, and through reductions in government debt. In fact, the net gains in revenue from the sales of the mines were obliterated, providing support to the empirical study of Buchs (2003: 11, 12) that found public finances did not improve in sub-Saharan Africa as a result of the privatisation of SOEs.

The failure of the privatisation of the copper mines to improve the public finances of the Zambian government was predominantly due to:

- the poor state of the ZCCM (largely owing to the lack of reinvestment in the mines) and the Zambian economy that diminished the bargaining leverage of the government, which significantly contributed to the concomitant reduced selling price of the mines;
- the extensive concessions granted to the mining TNCs, in particular the concession allowing TNCs to pay only a small portion of the total cash consideration at the conclusion of the sales of the mines. The rest of the cash consideration constituted deferred/conditional future payments;
- weaknesses in the institutional and regulatory measures during the privatisation of the mines that encouraged opportunistic practices;
- alleged corruption by government officials;
- the use of gross receipts from the privatisation of the ZCCM to pay the liabilities of the ZCCM; and

- the government's assumption of various liabilities of the ZCCM that was primarily responsible for the failure of the privatisation of the ZCCM to reduce the country's debt.

The blame for the poor gains in government revenue that the World Bank and the ZPA placed on the delays in the privatisation process of the mines that opens the debate as to whether a gradual or a rapid privatisation should be favoured is a misconception. This is because the delays did not initiate the corruption and degrading of the mining assets, but merely exacerbated them. Indeed, the rapid move to privatise the mines in the latter part of the 1990s, mainly due to pressure from the IMF and the World Bank and other donors, enabled opportunistic practices and the alleged corruption that marked the privatisation of the mines in Zambia.

Instead of a swift privatisation, a gradual process allowing for the strengthening of legal and institutional measures and for better planning of the privatisation, would likely have been more beneficial for Zambia. Moreover, rather than due to privatisation per se, the poor gains in government revenue from the sales of the mines were largely attributable to inadequate consideration given to the manner in which the privatisation proceeded. Poor institutions, which facilitated corruption, played a particularly negative role in limiting higher public finances from the privatisation of the mines.

7.2.3 Changing objectives and management structure under different ownership and the impact on mining performance and Zambia's socio-economic development

Main observations from the study were that changing objectives under different ownership affected the performance of the mining companies, and the socio-economic development of Zambia in distinct ways. Moreover, organisational weaknesses under government ownership of the mines also eroded the performance of the mines. The argument that better incentives improve company performance was unclear under government ownership but private management of the mines. Also, the neo-classical argument that more effective control of managers under private ownership, compared to

SOEs, further contributes to better performance of private companies, was less evident in the case study. An explanation of these conclusions follows.

The study found that the profit-maximisation objectives of the principals under private ownership of the mines (their shareholder) contributed to improved company performance, by way of higher worker productivity and a lower cost of production or *x*-efficiency, than was the case under government ownership. Based on the assumption that total revenue remained equal or increased under private ownership compared to government ownership, these improvements support the neo-classical argument that profit-maximising motives of private companies' shareholders contribute to the better performance of private-owned enterprises. In contrast, under government ownership of the mines, the electoral-maximising and multiple objectives of the state curtailed greater reductions in the costs of production and improvements in the productivity of workers.

On the other hand, as noted above, the electoral-maximising motives of the Kaunda government encouraged higher employment levels of mineworkers, and an improvement in the standard of living and welfare of the Zambian nation. However, the redistributive activities had a negative impact on the growth in the mining sector when the copper mines performed poorly. These outcomes vindicate the argument of neo-classical theorists that electoral-maximising objectives of the government limit better company performance.

Definitive conclusions on the role of ownership on production levels could not be drawn from the study. This is because the influences of various factors on production, the short span within which the private companies operate in the mines, and the positive impact of the unprecedented rise in copper prices on production levels under private ownership obscure such conclusions. Production levels, however, were high in the late 1960s and in the 1970s under government ownership of the mines, when the mines performed more effectively. However, in the absence of measures to increase growth in the mining companies to reinvest into the mining sector and to encourage the savings of a portion of mining surpluses, the state was unable to sustain high production levels.

Organisational weaknesses of the mines under government ownership, namely bureaucracy that obstructed quick decision-making and political influence introduced in the operations of mining companies, further accounted for the poor performance of the mining sector. In the short term, increased costs and lower productivity as result of Zambianisation policies because of reduced know-how and efficiency and a 'fragmentation' of skilled jobs also limited greater improvements of the copper mining companies. However this was not the case in the medium to longer term, as the very effective training policies provided to indigenous Zambians in fact significantly enhanced the skills of Zambian managers. The organisational weaknesses that the mining companies experienced under state ownership confirm the neo-classical perspective that lack of management autonomy, internal inefficiencies in bureaucracies and multiple and contradictory government objectives further account for poorer company performance under government ownership.

Under private ownership of the mines, the superior incentives provided to managers, brought the objectives of the principal closer to those of the agent. In contrast, poorer incentives provided to managers under government ownership dampened the motivation of managers to pursue greater profit-maximising objectives. The poorer incentives occurred as a result of lower wages, a reluctance of the government to replace managers who did not make a profit and the elevation of political interests and electoral-optimising objectives over profit-maximising motives in the government-dominated board. Although private managers enjoyed higher incentives it is not possible within the confines of the study to draw definitive conclusions on a direct relation between higher manager incentives and improvements in company performance.

Moreover, higher incentives failed to induce better performance of the copper mining companies in Zambia when the mines were under private expatriate management control but under government ownership (between 1970 and 1973). On the contrary, the higher costs that curtailed greater *x*-efficiency reduced further improvements in the performance of the mines under private foreign control of the mines. The high costs were largely owing to the manipulation of profits, through transfer pricing policies and also through high service fees charged by parent companies of mining TNCs that enjoyed exclusive rights in the provision of these services. The practices of the mining TNCs of repatriating a large portion of their share of profits, among others as dividends to their foreign shareholders, instead of using them for reinvestment in the mining sector, also led to a significant portion of mining surpluses leaving Zambia.

The failure to achieve greater improvements in company performance when the mines were under government ownership but under the control of private management discounts the view of property rights theorists that better incentives provided to managers would improve company performance. Accordingly, superior incentives provided to private managers per se were not a sufficient condition for improved company performance in the Zambian mining sector under government ownership of mining companies. Improved company performance during government ownership but foreign private management of the mines also required effective government controls to curb both transfer pricing practices and the externalisation of mining profits out of Zambia.

In more recent examples, the takeover constraint did not represent an effective deterrent against the poor performance of the private mining companies either. For instance, the poor performance of RAMCOZ under private ownership and the departure of Anglo American from Zambia did not result in a smooth takeover. A substantial delay of two years took place from the decision of Anglo American to withdraw from Zambia and the eventual resale of KCM to Vedanta, at the end of 2004. Moreover, delays and difficulties that the government experienced in getting new private sector interests to take over Luanshya/Baluba imposed a huge cost on the Zambian economy. This contradicts the argument of pro-privatisation proponents that superior monitoring and control of managers under private ownership, because of capital markets and the takeover constraints that are absent under government ownership, also account for the poorer performance of SOEs. Rather, these outcomes are consistent with the view of

Craig[700] that uncompetitive capital markets curtail the monitoring and control of private companies, rendering them ineffective as regulators of manager performance within private firms in developing countries.

Socio-economic costs of cost-cutting or profit-maximisation objectives of private companies

Several of the profit-maximising and cost-cutting measures of private TNCs that might have been necessary as a damage control exercise to improve company performance had a negative influence on the socio-economic development of the Zambian economy. Principal *x*-efficiency measures that impacted negatively on the socio-economic development of Zambia were: (i) the large concessions granted to mining TNCs; (ii) the reductions in the labour force and a lowering of their conditions of employment; (iii) the shifting onto the government of some responsibilities, such as the payment of retrenchment and pension packages, as well as the provision of social services and for the treatment of some pollution; (iv) temporary closures and withdrawals of mining companies; (v) measures supporting foreign suppliers over local suppliers; and (vi) a depreciation of the kwacha.

The reductions in the costs of production of private mining TNCs through lowering permanent employment levels, degrading the conditions of work of mineworkers and through diminishing the provision of social services of the mining community degraded the welfare of the nation, increased poverty levels and polarised wealth in favour of mining TNCs. The de-industrialisation of the local economy further contributed to increases in poverty levels. Moreover, enormous costs imposed on the government (owing to concessions granted to TNCs and its assumption of various liabilities of the mines and for the maintenance of non-core mining services, previously performed by the ZCCM) and the volatile exchange rate had a highly negative impact on the Zambian economy. Various problems evident in the privatised setting were, however, also attributable to failures in government regulations and in their implementation.

700 Cited in Cook and Kirkpatrick, 2000b:17.

Accordingly, the benefits of several cost-cutting and profit-maximising measures of private companies to improve company performance need to be weighed against their socio-economic costs for the Zambian people. The poor socio-economic outcomes under private ownership of the mines support the argument of Kiken (1998) that the tendency of private enterprise to neglect the economic, political and social consequences of their activities in lower-income economies might undermine sustainable improvements in the standard of living and the welfare outcomes. In such instances, the economic growth, distribution and poverty effects of privatisation may not necessarily be positive (cited in Kirkpatrick & Parker, 2005:529; Cook & Kirkpatrick, 2000b:24).

7.2.4 Political-economic implications of the privatisation, changing ownership and government policies of the mines and the impact on development

In the absence of various prerequisites for a more successful privatisation and a greater redistribution of gains from improved company performance, privatisation and private ownership tended to undermine the socio-economic development of the country. The flawed manner in which the mines were privatised, marked by poor governance, likely benefited the senior government officials that were allegedly involved in the corruption that transpired during the privatisation of the ZCCM. On the other hand, the losses in revenue from corrupt practices, poor sales prices, concessions granted to mining TNCs and the government's assumption of the huge liabilities of the ZCCM negatively affected the Zambian economy, in loss of revenue. Moreover, the inadequate protection of the interests of mineworkers impeded a greater redistribution of benefits of the privatisation of the mines to the mineworkers.

A major shift occurred in the political economy under private ownership of the mines from what was the case under government ownership of the mines. Under private ownership of the mines, profit-maximising objectives and the poor redistribution of gains from mining, together with an ineffective enforcement of existing legal measures governing private ownership of the mines concentrated gains from mining mainly with the private mining TNCs, their shareholders and foreign suppliers. Conversely, the deficiencies in government policies and especially the cost-cutting measures of the private companies to achieve *x*-efficiency objectives had a detrimental influence especially on the local mineworkers, the Zambian-based suppliers to the mines and the Zambian economy, limiting development gains for the country.

In contrast, under government ownership of the mines, the main beneficiaries of Kaunda's redistributive policies in the mining sector were the Zambian mineworkers, the local managers that took over from the expatriates[701] (with the assistance of the Zambianisation policies) and the mining community. The welfare of the mining community improved considerably due to the greater accessibility of social services under Kaunda's rule. Moreover, the protectionist policies that the Kaunda government instituted and the reallocation of mining revenue to develop the local manufacturing sector were highly beneficial to the locally-based industries to the mines. However, the manufacturing sector had several limitations. For example, their poor inter- and intra-industry linkage that rendered these industries highly dependent on intermediate inputs and their lack of competitiveness eclipsed the scope and sustainability of the local industries.

On the other hand, under the MMD government a significant change took place in the political economy of Zambia (already before the privatisation of the mines), following its rigorous adoption of the SAPs and liberalisation policies imposed by the IMF and World Bank. As is noted above, in the absence of creating alternative employment to absorb the unemployed workers, the high number of retrenchments of workers as a result of demand management measures had a negative impact, especially on those mineworkers left unemployed. Demand management programmes further degraded the social services of the Zambian community. Supply-side measures and free trade policies affected especially the local suppliers adversely. Conversely, the SAPs and liberal policies predominantly favoured the private mining TNCs, the foreign suppliers and the expatriate managers.

[701] Expatriates were from the countries of origin of the mining TNCs.

7.2.5 Recommendations for more beneficial privatisation of SOEs

Measures that would have promoted greater advantages for Zambia from the privatisation for the mines include:

- More gradual and effective planning of the privatisation of the mining sector to allow for:
    - The building of stronger and more competent institutions and a rigorous regulatory framework, before the mines were privatised, as well as for better monitoring and enforcing of regulations. Such measures would have been more effective in curtailing non-transparent activities and corruption and negative consequences of privatisation on the Zambian economy.
- Government-introduced safety nets and redistributive measures needed to promote better outcomes for the mineworkers and the mining community, namely:
    - Alternative employment creation, before the mineworkers were retrenched, to absorb 'surplus capacity' as a result of privatisation policies.
    - The provision of adequate social security to the mining community and unemployed mineworkers that were negatively influenced by the privatisation of the ZCCM.
- Measures ensuring higher government revenue from the privatisation of the ZCCM through:
    - A higher bargaining leverage of the government.
    - Better performance of the Zambian economy and of the ZCCM, partly through greater reinvestment within the ZCCM before it was privatised.
    - Demanding the total cash considerations from mining TNCs immediately at the conclusion of the sales of the mines, rather than granting private mining companies deferred cash considerations.
    - Limiting the time-frame of investment obligations of mining TNCs.
    - The state refraining from assuming the debt of the ZCCM, including the payment of retrenchment packages of many mineworkers that lost their jobs, partly as a result of some mining TNCs making these demands conditional on the conclusion of the sales of the mines.

- Curbing corruption during the privatisation of the mines, through stronger institutions and regulations.
- Increasing mining companies' taxes, which are limited by the concessions granted to the mining TNCs. Privatisation has been less decisive than profound tax administration reform for revenue performance (Buchs, 2003:12, 13).

- Redistributive measures to ensure a greater 'trickle down' of the benefits of improved performance of private mining companies to local Zambians. In the absence of such measures greater *x*-efficiency and profit-maximising objectives of private companies might in fact disadvantage the local Zambians.
- An exploration of alternatives other than the privatisation of the mines, in light of the strategic importance of mining to the Zambian economy and because of the highly negative impact that the privatisation of the mining sector has had on the socio-economic development of Zambia.
  - A corporatisation of the mining sector, allowing for a continuation of government majority ownership but under private-sector management, and in some cases a private-sector minority stake in the mines. Government ownership would have constrained the leakages of profits out of Zambia, while private management would have limited both the political influence of the government and its tendency to over-extend the resources of the mining sector into unproductive sectors.
  - Measures ensuring higher Zambian private sector participation in the ownership of the copper mines that would have enabled a greater redistribution of benefits to the locals from the privatisation of the ZCCM.
  - Greater reinvestment in the mines before they became cash-strapped, which would have enhanced the capacity of the government to augment the performance of the ZCCM under government ownership.
  - A significant reduction of Zambia's external debt, also under government ownership of the mines. The reduction could possibly have been on a similar basis to the HIPC initiative and the MDRI that Zambia qualified for recently when the mines were under private ownership.

7.3 THE ROLES OF TNCs IN THE MINING SECTOR OF ZAMBIA (WITHIN A WEAK STATE)

Significant findings that emerged from the assessment of the roles of TNCs in the mining sector of Zambia were first that their technological and capital inputs in the mines were their principal contributions in the development of Zambia. Second, the bargaining leverage of the government against those of the mining TNCs played a crucial role in determining the outcomes of the participation of these TNCs in Zambia. Third, in the short term, significant reductions in government revenue and foreign exchange obtained from mining and an erosion of certain benefits of local suppliers and workers under TNCs' ownership of the mines severely eclipsed the transfer of greater returns for Zambia from the surpluses of mining under the TNCs' ownership of the mines. Fourth, factors other than concessions and liberal policies were more dominant in influencing the locational decisions of the mining TNCs in Zambia. Furthermore, the activities of the TNCs in the mining sector, together with the more extensive and liberal policies that the Chiluba government adopted, and the poor capacity of the Zambian government altered the political-economic landscape of the mining sector and the Zambian economy. These findings are explained in the next sections.

7.3.1 The roles of TNCs in supplementing technology and capital

The notable contribution of TNCs in augmenting much needed technology and capital stock of the copper mines in Zambia enabled greater exploration of minerals, the opening of unused mines and the development of the mining sector. The capital and technological input were crucial especially in light of the poor recapitalisation of the mining sector in the late 1990s, which was a major contributing factor of their weak performance. The significant contribution of virtually all the mining TNCs, with the exception of Binani, in increasing the technology and capital stock of the mining sector validates the neo-classical[702] and neo-fundamentalists' views[703] that TNCs play a pivotal role in supplementing the capital and technology of the host country (cited in Helleiner, 1989:1451; Jenkins, 1987:19, 20, 32).

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702 See, for example, proponents of the product cycle model (Vernon, 1979) and of 'internalisation' (Buckley, 1985 and Casson).
703 See, for example, Warren, 1980 and Emmanual, 1976.

However, despite considerable investment by the mining TNCs that took ownership of the mines compared to that under government ownership in the mid-1990s, in the short term their investment levels were lower than what were pledged in the development agreements. In fact, the investment levels of these TNCs were less in real terms over the short term under private ownership from 1997-2003, than the average investment levels from 1990-96, under government ownership. Moreover, within a weak state, investment from the mining TNCs in Zambia was significantly influenced by factors such as the price of copper, their practice of delaying investments and the excessive concessions granted to them. In particular, the concession allowing for pledged rather than definite investments from mining TNCs enabled the delaying of their investment commitments. Moreover, the reliance of several mining TNCs on existing mining operations in Zambia, instead of on their foreign sources to finance the development of greenfield projects that they have pledged to develop further limited the scope of their capital inputs in the host countries.

Accordingly, in the short term the impact of all these factors on investments considerably contributed to the fluctuations in investment levels under TNCs' ownership of the mines. However, in the longer run, improved company profits as a result of greater efficiencies pertaining to private ownership of the mines could encourage higher investments in the mining sector. The poor bargaining leverage of the government over those of mining TNCs and certain weaknesses in the institutional, regulatory and the implementational capacity of the government also curtailed the extent of the technological and capital transfers from mining TNCs to the mines.

Furthermore, the activities of Binani at RAMCOZ in Zambia demonstrate that TNCs do not always transfer capital and technology to the host country. In fact, various activities of Binani, together with the government's subsequent assumption of the role of receiver of the company, amounted to a draining of the resources of TNCs, at great cost to the state coffers. Most notable among these activities were Binani's failure to pay its huge liabilities to the national bank, suppliers, workers and statutory bodies in Zambia (for which the Zambian government largely assumed responsibility), and its asset-stripping activities. These activities of Binani contradict the neo-classical argument that TNCs have a positive role in host countries, while affirming the counter-perspective of the Global Reach and neo-imperialist theorists that TNCs drain the resources and undermine the development of the host country. However, the alleged corrupt relationship that the Chiluba government had with Binani probably abetted some of the actions of the mining company.

Despite lower investment levels than were pledged and the practice of TNCs to raise capital locally rather than internationally, in the late 1990s however, under state ownership of the mines, the government would unlikely have obtained sufficient capital required to reinvest in the mines. The diversion of mining revenue for developing other sectors to fulfil the multiple objectives and electoral-maximising motives of the government, alongside the huge debt of the country and the poor performance of the ZCCM especially in the 1990s, severely limited greater investment in the mines under government ownership. External factors, in particular IMF and World Bank policies barring higher government investment in the mines earmarked for privatisation from 1996, were also significantly responsible for huge reductions in investment in the mines in the late 1990s, under government ownership.

7.3.2 The bargaining position of the government over mining TNCs (and primary consequences)

The opportunistic manner in which the mining TNCs conducted themselves is fundamentally also a function of the poor leverage of the Zambian government over those of the mining TNCs. Most significantly, the weak bargaining position of the government enabled the mining TNCs to consolidate their advantages in the mining industry by collaborating through the Kafue Consortium during the bidding process for the final and most lucrative assets of the ZCCM. It further enabled the mining TNCs to obtain excessive concessions from the government. In turn, the government imposed very few obligations on the mining TNCs.

The formation of the Kafue Consortium reduced competition and enabled the consortium to undervalue the assets of the ZCCM it was to gain during the bidding process and to demand highly favourable terms from the government. The weak economic position of the country and the poor capacity of the government to value the mines independently of the advisors and of the buyers, and to assert higher prices for the mines enabled the mining TNCs to adjust bids in their favour. Moreover, the concessions granted to mining TNCs dramatically reduced government revenue from mining.

The strong leverage of mining TNCs to act opportunistically points to weaknesses in the argument of the bargaining proponents that governments are able to influence the activities of TNCs towards advantageous outcomes for the host country. On the contrary, it demonstrates that a weak state and liberalised economy significantly limited the government's ability to dictate terms to the mining TNCs that would optimise its returns from mining. This, together with the failure of liberal policies that the Chiluba government adopted in promoting greater benefits for Zambia from the activities of mining TNCs, affirms the argument of development theorists (such as Leftwich, 1995:415; Kim & Leipziger, 1993:29, 30) that a strong government bargaining leverage is pivotal in enabling the government to direct the activities of TNCs to more favourable outcomes. A strong bargaining leverage of the state (a corporatist role) over those of the mining TNCs is also crucial to ensure that the greatest possible share of the rent element from mining accrues to the host country (Chang, 1998:238).

7.3.3 Returns to the Zambian economy from the extraction of copper

The confining of the government's revenue base from mining to mining tax revenue under private ownership of the mines, alongside the finite benefits pertaining to exhaustible resources, necessitates the optimising of tax revenue under private ownership of the mines to ensure the maximisation of returns for the government from mining. Under government ownership of the mines, government income from mining was obtained both from mining tax and directly from sales and profits from the mines. The externalisation of surpluses from mining under the TNCs' ownership of the mines also reduced the foreign currency reserves obtainable from mining for Zambia. Moreover, reinvestment of a proportion of mining rent into non-exhaustible resources, including the development of human capital and of lateral sectors to mining, is necessary to ensure more sustainable development from mining (see, for example, Blignaut & Hassan, 2002:89-101; Blignaut & Hassan, cited in Cawood *et al*., 2001:157; Pedro, 2004:6).

7.3.3.1 Government tax revenue from mining

In the short term, the large concessions granted to mining TNCs on corporate tax, VAT, duty tax, mineral royalty tax and other taxes, virtually obliterated instead of optimised government taxes from mining under private ownership of the mines (until 2004). Even during the copper price boom, from 2004 to 2007, the taxes from mining were still considerably lower than those in the early 1990s. Conversely, under TNCs' ownership of the mines the tax burden was shifted away from the private mining TNCs to the Zambian population, through increases in VAT and non-tax revenue of Zambians, and especially to the mineworkers through PAYE. The government's share from mining declined, also during the years of the copper price boom, despite the general increase in total government revenue in subsequent years.

However, the limited gains in government revenue under TNCs' ownership of the mines were not owing to an inherent flaw in the operations of TNCs in host countries. Rather, these arose significantly as a result of the poor bargaining leverage of the host government that enabled the mining TNCs to extract excessive concessions from the government. Additionally, weaknesses in certain laws and in their enforcement obstructed a greater capturing of mining surpluses for the government. The inclusion in the constitution of certain clauses of development agreements providing for incentives continues to limit reductions in concessions. This is because their inclusion in the constitution makes compliance to the concessions legally enforceable and subject to an international arbitration process. The difficulty the government experienced in enforcing additional tax increases proposed in the new Income Tax Amendment Bill (Act 1) of 2008 that subsequently obliged it to reverse some of the tax increases demonstrates the obstacles the government faces in reducing concessions.

7.3.3.2 The repatriation of mining resources and foreign currency earnings from mining

The significant repatriation of mining surpluses that increased dramatically during the boom in copper prices (from 2004 to 2006) under private TNCs' ownership of the mines, as well as through possible transfer pricing policies, further limited the capturing of rent from mining by the MMD government. The resultant reduction in returns for the Zambian economy from the surpluses obtained from the extraction of copper reduced gains through investment and tax revenue under TNCs' ownership of the mines. It also curtailed greater savings from mining activities for the Zambian economy. High reductions in returns for the Zambian economy under TNCs' ownership of the mines relative to benefits in technological and capital inputs would cancel gains from the participation of mining TNCs and could amount to a draining of the resources of Zambia.

The repatriation of mining revenue also caused volatility and sudden outflows of foreign exchange, which are likely to continue their destabilising impact both on the level of Zambia's foreign currency reserves and on the exchange rate. Weaknesses in government policies also facilitated the repatriation of surpluses from mining. In particular, the weak control over securities and exchange and the absence of exchange controls enabled the repatriation of all after-tax profits from mining under the TNCs' ownership of the mines.

7.3.3.3 The roles of TNCs in promoting the development of local capital

The activities of TNCs did not promote significant improvements for local capacities, namely the locally based suppliers and the mineworkers, either. The improvements in the short term in the growth and employment of local suppliers under private TNCs' ownership of the Zambian mines (due to the greater ability of the mining TNCs to pay the local suppliers than was the case immediately prior to the privatisation of the mines) were at levels still lower than those of the early 1990s. Certain practices of the mining TNCs in fact considerably offset and at times undermined greater improvement in the development of local suppliers.

In particular, the continued practice of the mining TNCs to replace local suppliers in the procurement of mining inputs with cheaper and mostly better quality imports from foreign manufacturers and suppliers, allegedly also from their own foreign subsidiary supplier companies, has limited higher growth in the manufacturing sector. The poor participation of local suppliers in the inputs of mining also precluded a greater transfer of technological know-how from TNCs to the local suppliers. However, certain inefficiencies of local companies and weaknesses in government policies reinforced these trends.

As far as the mineworkers are concerned, a large reduction in the labour force under TNCs' ownership of the mines, mainly at the major operational copper mines, led to a significant overall decline in the short term in the employment levels of the mines. This was in spite of the higher employment opportunities for mineworkers in those mines that re-opened. Permanent mining employment declined from 47 700 in 1996 immediately prior the privatisation of the mines to 19 000 in 2002.

The cuts in excess capacity in the labour force might have been a necessary damage control exercise to improve the performance of the loss-making mines. However, the reductions in permanent employment also appear to be a strategy to enable an increasing shift of permanent workers into non-permanent employment. This was mainly achieved through the increasing use of foreign contractors. Non-permanent workers enjoy much lower conditions of employment than permanent employees, mostly through lower wages, lack of pensions and union representation. Moreover, the rise in total employment in the mining sector during the boom in copper prices from 2005-07 (from the 2001 levels) were still considerably lower than the levels in the early 1990s.

Moreover, insufficient training of local workers at several mining companies limited the transfer of skills from TNCs to the local capacities. Such skill transfers are highly beneficial in developing the human capital of the host country, according to various theorists (see, for example, Padayachee, 1995:173 and Stiglitz, 1998:25, 26, 32).

Human capital development, in turn, possesses enormous potential for speeding up the development of host countries. The replacement of many Zambian workers with foreign workers and Zambian managers with expatriates (from the countries of origin of mining TNCs) at most of the mining companies under the TNCs' ownership of the mines, further reduced advantages for the affected parties. Various loopholes in government measures also accounted for the poor benefits to local capacities from the activities of mining TNCs.

7.3.4 Factors influencing the decisions of mining TNCs to depart from Zambia

The study found that the concessions and liberal policies proved insignificant in determining the locational decisions of mining TNCs, contradicting the argument of Rugman that unrestricted trade and industrial policies are crucial for attracting TNCs (cited in Jenkins, 1987:22). Other economic factors, especially the global profit-maximising objectives of the parent companies of mining TNCs, the competitiveness of Zambia in relation to other countries and the quality of minerals in the mining sector proved more fundamental in determining their locational decisions in Zambia. The decision of Anglo American to depart from the country is a case in point.

The lower competitiveness of Zambia was mainly as a result of the high-risk perception of Anglo American's shareholders of African investments, the relatively high production costs and the greater inaccessibility of Zambia's copper, which requires deep-level mining, whereas open-cast mining (that is cheaper to extract)[704] is predominant in Chile. Moreover, losses and liquidity problems that both Anglo American and AVMIN experienced contributed further to their decision to depart from Zambia. The failure to win the Luanshya/Baluba bid, which would have secured Chambishi Metal's long-term feasibility, was also highly significant in influencing AVMIN's decision to depart. Weaknesses in laws, considered in Section 7.3.5 below, further facilitated the exit of Anglo American from Zambia.

[704] Mainly due to construction of costly sink shafts necessary to reach the ore in deep-level mining.

7.3.5 The political-economic implications of the state's regulatory and institutional capacities governing mining TNCs and of mining TNCs' activities

Under the TNCs' ownership of the Zambian mines, within a weak state, the power asymmetry between the Zambian government and mining TNCs enables the mining TNCs to behave opportunistically and to skew gains over investments and the returns from copper mining in their favour. Consequently, the mining TNCs, their shareholders, the foreign suppliers of mining inputs in Zambia and expatriate managers that are preferred over local managers are mostly favoured. On the other hand, the local mineworkers (that were largely advantaged during Kaunda's administration), the local suppliers to the mines and the Zambian economy continue to be adversely affected by several practices of mining TNCs.

The various weaknesses in government policies, laws, institutional and enforcement capacities regulating the activities of mining TNCs, and donor driven economic policies that the government was forced to adopt mainly due to its huge external debt, reinforced these trends. These weaknesses benefited mainly the mining TNCs, often at the expense of the Zambian economy and local capacities, viz. the mineworkers and the Zambian-based suppliers. Most important weaknesses in the government measures were firstly, the deficiencies in government policies limiting higher technological and capital inputs of mining TNCs. These included: (i) the general inability of the government, primarily due to its weak bargaining position, to set the terms of TNCs' investment obligations in the mining sector; (ii) the concession allowing for pledged rather than definite investments; (iii) clauses in the development agreements entitling TNCs to a proportional reduction of their capital expenditure commitment in the short term, and to close or significantly curtail operations, subject to the viability of their operations; (iv) the sanctioning of deferred cash payments to mining companies; and (v) the non-recourse nature of investment commitments of TNCs in Zambia.

Secondly, the significant concessions granted to mining TNCs through the Investment Act (1995), the Mines and Minerals Act (1995) and bilateral development agreements between the government and the mining companies favoured mining TNCs.

Concomitantly, these policies deprived the government considerably of higher revenue from the rent element from mining. Thirdly, the lack of an exit clause for the mining TNCs and, in the short term, the low sunk costs[705] of mining TNCs facilitated the exit of mining TNCs from Zambia. Higher sunk costs of the TNCs would also have improved the bargaining leverage of the Zambian government, among other factors, to make greater demands on the mining TNCs.

Fourthly, poor industrial policies and weaknesses in regulations governing the relation between local suppliers and the mining TNCs under Chiluba's government contributed considerably towards undermining the development of locally-based suppliers. Liberal policies largely precluded the development of industrial policies necessary to promote local industries. This vindicates the argument of Fine and Stoneman (1996:19) that the minimalist government policies subsumed in liberal policies favoured by the IMF and the World Bank are not neutral. Rather, these policies have especially advantaged private capital. In particular, foreign suppliers are largely benefiting from these deficiencies in government policies and from practices of mining TNCs to replace several local suppliers with foreign suppliers.

Broadly, the weaknesses in the industrial policies under MMD rule precluding greater advantages for local suppliers from the participation of mining TNCs in Zambia encompassed:

- failure by the government to protect local suppliers against the practice of mining TNCs of replacing them with foreign suppliers;
- excessive foreign investor-friendly policies not extended to local companies;
- liberal policies that facilitated the substitution of locally-based industries in the supply of mining inputs;
- omissions in agreements obliging mining TNCs to support local suppliers; and
- agreements allowing mining companies to choose their own suppliers.

[705] A cost that has been incurred and cannot be reversed (Investopedia, 2010).

Moreover, a failure to encourage vertical and horizontal linkages between the global mining TNCs and local capacities deprived Zambian suppliers and mineworkers of significant benefits pertaining to the transfer of technology and know-how to local capacities. The transfer of knowledge from TNCs would have played a pivotal role in augmenting the human capital development of Zambians. Other factors, in particular insufficient capital and the high costs of production of local suppliers, also adversely influenced these suppliers and need redress to improve their competitiveness.

Fifthly, various weaknesses in the legal and enforcement capacity of the government in promoting the development and protection of mineworkers have made it possible for mining TNCs to lower gains to the mineworkers, especially by way of the reductions in permanent employment and of their conditions of work. Additionally, poor implementation of labour regulations limiting the displacement of local workers with foreign workers and weak protection of workers to organise collectively also disadvantaged local mineworkers. The non-obligatory nature of clauses in the development agreements to aid the retrenched workers in gaining alternative skills and weaknesses in certain clauses on the training of local Zambians and the employment of local workers further limited the employment opportunities of Zambians. Moreover, the weak capacity of formal regulatory bodies to protect the safety of mineworkers undermined better safety standards for mineworkers.

The shift in benefits away from workers is consistent with the argument of Bond and Manyanya (2002: 62, 63, 71, 79) that an increasing acceptance of IMF and World Bank policies, together with corrupt practices, signify a realignment of the government away from the more marginalised communities (workers included), which especially favour foreign capital and the government elite. The poor development outcomes for Zambia, significantly as a result of a weak state capacity, validate the arguments of theories of the developmental state that favour a greater interventionist role of the state. The prerequisites that accounted for the high state capacities and concomitantly for the enviable progress of developmental states were largely lacking in Zambia. Some of these measures that Zambia could draw from, include economic bureaucracies that enjoy power and competence and are insulated from the influences of other interest groups, a corporatist role of the state and effective industrial policies.

7.3.6 Recommendations of government measures necessary for greater benefits for Zambia from mining TNCs' activities

The measures necessary to direct the activities of mining TNCs towards more advantageous outcomes for Zambia require:

1. The redressing of various deficiencies in the laws governing the activities of mining TNCs to curtail the harmful consequences of the activities of mining TNCs to the country, whilst steering their activities towards greater benefits for Zambia. These would necessitate the government:

   a. Encouraging greater investment of mining TNCs in Zambia through:

      - Setting the terms and enforcing investment obligations of mining TNCs.
      - Limiting tax holidays that significantly curtail increased investments in Zambia. This would require the government eliminating clauses in the development agreements allowing mining companies to reduce their capital expenditure commitments at their discretion, or to temporarily or permanently close their operations and to defer their cash payment commitments.
      - Ensuring that TNCs possess sufficient funds, before investing in Zambia, rather than employing profits from existing mines to develop new mines.
      - Demanding definite rather than pledged investment obligations that have to be determined during the bidding process.
      - Linking investment commitments to have recourse to shareholders of the mining TNCs.
      - Ensuring that the investments of mining TNCs exceed the repatriation of their profits out of the country.

   b. Providing the country with greater protection against withdrawals of mining TNCs. Withdrawals of mining TNCs from Zambia could have been curtailed by:

      - The introduction of a considerable exit penalty in agreements, penalising mining TNCs should they withdraw from Zambia.
      - Linking the activities of TNCs to have recourse to their shareholders.

- Ensuring that TNCs incur greater sunk costs, by way of higher investments in Zambia, soon after their takeover.

2. A greater capturing and redistribution of returns by the government from mining TNCs to the Zambian economy through the government:

   a. Prompting TNCs to reinvest a greater portion of their profit in Zambia.

   b. Increasing its shares in the mines.

   c. Renegotiating with mining TNCs to reduce their concessions. Higher corporate and other taxes on mining companies seem necessary to ease the high tax burden on workers and on the Zambian population, and to enable greater benefits for the country from the surpluses from mining.

   d. Limiting the repatriation of profits and resources of mining TNCs out of Zambia (also through dividends).

   e. Introducing laws in the financial sector to curb the high repatriation of foreign currency earned from mining. These would include measures obliging the mining TNCs to deposit or exchange (for the local currency) a higher portion of foreign currency acquired from copper sales with the Bank of Zambia to improve the foreign currency reserves of the country.

   f. Ensuring greater accessibility of social services to Zambians and their adequate maintenance under private ownership of the mines, through the government:

   - Transferring the responsibility for the provision of these services and for the upkeep of mining townships[706] to the mining companies.
   - Specifying in the development agreements that mining TNCs provide all the services that the ZCCM previously provided to the mining community.

3. Government measures promoting the development of local suppliers under TNCs' ownership of the mines:

   a. State-directed investment that pertains to developmental states to promote more favourable outcomes for local suppliers from the participation of mining TNCs in the Zambian economy requires:

   - An industrial policy promoting the development of local suppliers, by way of protectionist policies, through the use of subsidies, taxes and tariffs whilst at

[706] That were transferred to the ill-resourced local municipal authorities.

the same time encouraging local industries to become internationally competitive.

- The elimination of government policies that undermined local suppliers, such as the excessive foreign investor-friendly policies, especially the concessions granted to foreign companies. Policies that place high import duties on raw materials and intermediary products and that reduce duties on finished goods, which sabotage the local manufacturing sector, should be reversed.
- Government industrial policies obliging TNCs to provide greater support to local suppliers.
- The establishment of vertical and horizontal linkages between local suppliers and TNCs that hold significant potential benefits for the development of the host country.
- The development of local forward linkages or value-added products to the copper mining sector, also other than smelting (where most of the forward linkages of mining is concentrated),[707] in which Zambia has a comparative advantage.[708] Policies that would promote forward linkages to copper mining include:
    - Incentives and supplying the local manufacturers that need copper inputs with a certain percentage of copper cathodes from copper mining companies.
    - The introduction of higher export duties on copper concentrates.
    - Lower charges for the treatment of copper concentrates that would create an economic incentive for mining companies to smelt copper or to process these concentrates in Zambia (Fraser & Lungu, 2007:4, 17, 60).
- Measures curbing practices of mining TNCs to substitute locally-based suppliers with foreign suppliers.
- The government limiting the adoption of liberalisation policies before or alongside the privatisation of the mines at a time when local capacities are weak and when markets are highly imperfect. In particular, free trade

[707] As most of Zambian copper ores are concentrated and smelted in Zambia and a number of new smelters are being built.
[708] Namely; electrical products (copper wires, electrical plugs, pipes) and other light-industrial goods.

policies, as well as the liberalisation of the capital market and the exchange rate undermined local manufacturing companies in Zambia.

b. Low interest rates would enable greater local participation in the supply of inputs of the mines under private ownership.

c. Greater inter- and intra-industry linkages of Zambia's industries. Such linkages should have been in place before liberalisation policies were introduced. They would have reduced the high dependence of local industries on imports for intermediates and ensured more beneficial consequences for local suppliers from the depreciation of the local currency.

4. Greater protection of local workers against certain activities of mining TNCs that would be enhanced through the government:

a. Curbing practices of TNCs to increasingly shift permanently employed workers into contract and casual employment.

b. Limiting the employment of foreign workers.

c. Ensuring greater Zambian participation in the management structures of the mining TNCs.

d. Adopting measures obliging TNCs to transfer skills to Zambians, through training local mineworkers, to make them more employable. Furthermore, training provided by mining TNCs is important to promote the development of Zambia's human capital.

e. Strengthening the government institutions and other bodies overseeing the protection of workers, such as the Ministry of Labour and those bodies regulating the safety of workers (including the Mines Safety Department). This would enable a better enforcement of workers' rights.

f. Reforming labour legislation that would strengthen trade unions.

g. Addressing the weaknesses in the bankruptcy law in Zambia that shield liquidated companies from paying terminal benefits to workers.

5. A higher government capacity. This would be achieved through:

a. Competent economic bureaucracies necessary to implement government policies more effectively. This requires the:

- Reintroduction of long-term development plans to guide development.

- The establishment of more effective networking structures between state and non-state actors, at the national, provincial, district, and sub-district level.
- Strengthening of the capacity of institutions taxed with enforcement and monitoring the operations of TNCs through:
  - The provision of adequate resources, such as sufficient and competent manpower.
  - Better access to information as to the obligations of the mining TNCs to Zambia, partly through greater transparency of development agreements.
  - Swifter penalisation of malpractices by TNCs.

b. The promotion of a greater corporatist role of the government by way of:

- Measures raising the bargaining leverage of the government, which would have increased its capacity to work more independently of other stakeholders and improved its leverage in dictating terms to TNCs. A higher bargaining leverage would have been better accomplished through the government first consolidating its power, before the mines were privatised.
- The government limiting the influence of foreign donors on the Zambian economy.

c. The establishment of effective industrial policies to promote the local industrial sector, also backward- and forward-linkages to the mines.

6. The employment of mining tax revenue to diversify the economy to alleviate the 'Dutch disease' from which the Zambian economy is suffering, owing to its immense dependence on the mining sector.

7.4 CONCLUSION

Key features identified from the examination of the mining policies of the Kaunda and Chiluba governments are that the redistribution of mining surpluses, motivated strongly by the electoral-maximising objectives of the Kaunda government, played a crucial role in promoting the socio-economic and welfare development of Zambians. These policies further reduced inequalities that featured strongly in the Zambian economy under Federal rule. However, economic growth is a fundamental prerequisite for both reinvestment in the mining sector and sustainable redistribution. In the absence of sufficient growth, the allocation of mining surpluses into unproductive sectors has rendered redistribution of mining resources unsustainable in Zambia.

Furthermore, the protectionist industrial policies that the Kaunda government adopted proved fundamental in the notable development of the manufacturing sector, albeit from the very low base that prevailed at independence (and with several limitations). However, the failure of the government to incorporate measures alongside its protectionist policies that encouraged higher competitiveness of local industries, prevented an acceleration of the development of the local industries beyond their infancy stage (also backward-linked industries to the mining sector). Additionally, poor linkages between the industrial and mining sectors and the concomitant high dependence of the locally-based industries on imports for intermediary inputs severely diminished the scope of the mining sector as an engine of growth for the manufacturing sector.

The introduction of SAPs and strict liberal policies that the IMF and the World Bank imposed on the MMD government, in particular, the application of demand- and supply-side measures and liberal policies, without sufficient protection provided to local capacities, severely undermined especially the mineworkers and suppliers to the mines. The movement from low productivity towards zero productivity, as a result of the bankruptcy of many backward-linked companies to the mining sector in Zambia (especially following the introduction of trade liberalisation policies in the 1990s), reduced the benefits to the country (Stiglitz, 2002:59). The liberal policies were contrary to the policies of developmental states that encouraged industrial policies involving strong and effective state-directed investments that promoted local capacities (Leftwich, 1995:410; Amsden, 1997:469, 470).

The main findings identified from this study on the privatisation of the mines are that net benefits from privatisation are not inevitable. On the contrary, Zambia failed to improve its public finances from the privatisation of the mines. The zero gains in public finances from the privatisation of the mines were also significantly attributable to the weak state capacity of the Chiluba government. The weak state capacity enabled corrupt practices and forced the government to provide concessions to the bidders, and to assume the liabilities of the ZCCM. On the other hand, rather than privatisation per se, the mode of privatisation, which is not neutral, strongly determined the economic and the political-economic outcomes of the privatisation of the Zambian copper mines. This points to the need for establishing several prerequisites before privatising the mines, that would have guaranteed greater advantages for Zambia (from their privatisation). As is noted in Section 7.2.1.1, these include robust legal and institutional measures (also better monitoring and enforcement of obligations of private companies) ensuring greater gains for the Zambian economy, as well as the creation of alternative employment and safety nets protecting Zambians against negative influences of privatisation and the private ownership of the mines.

Furthermore, a better planned privatisation, invariably more successfully achievable through a gradual process to facilitate the establishment of these prerequisites before the mines were privatised, would likely have been more appropriate than the swift privatisation that the IMF and World Bank favoured. A stronger bargaining leverage would also have enabled the government to gain more from the privatisation of the mines. In the absence of the various prerequisites, the opportunistic practices that have strongly featured during the privatisation of Zambia's mines are likely to replicate.

Important elements identified from the assessment of the state and private ownership of the mines are that company performance improved under private TNCs' ownership of the mines (in the case of Zambia mainly through greater productivity and *x*-efficiency). However, improved company performance is a necessary but insufficient ingredient for sustainable development. In the absence of adequate redistributive measures of mining profits, improved company performance did not result in higher development gains for Zambia. On the contrary, in the short term, several cost-cutting measures of private companies promoted poor socio-economic outcomes. This was expressed in increases in the unemployment rate, and reduced welfare that escalated inequalities of wealth and poverty levels. Wealth though concentrates in favour of the private mining TNCs.

Accordingly, jobless growth (in the case of Zambia especially pertaining to permanent employment), despite increases in GDP growth and the huge profits of mining TNCs from the boom of copper prices, did not translate into meaningful development for Zambians.

A weighing of the advantages of improved *x*-efficiency against the socio-economic costs of profit-maximising measures on the Zambian population and economy provides a more accurate assessment of benefits for Zambia under private ownership of the mines, compared to the partial picture that a simple growth- or company performance-based determination of benefits provides. A correct balance between growth in the mining sector and a redistribution of mining surpluses seems paramount for the sustainable and more equitable development of Zambia.

Better incentives of private managers likely contributed to the improved performance under private ownership of the mines. However during the 1970-73 period, transfer pricing practices and the repatriation of a significant portion of surpluses to mining TNCs' parent companies rendered private management under majority government ownership of the mines insufficient for significantly improving company performance. However, government oversight enabled such practices from private expatriate managers. Furthermore, the takeover constraint was not an effective deterrent against the poor performance of RAMCOZ under private ownership, nor did it ensure a smooth takeover following the departure of Anglo American from Zambia. A delay of two years followed before Vedanta Resources took over KCM.

Furthermore, this study demonstrates that the minimalist role of the state that the IMF and the World Bank favour has reduced the capacity of the government to implement policies that would have been more advantageous to Zambians during the privatisation and under private ownership of the mines by TNCs. A minimalist state role is largely contained in liberal policies that the Chiluba government adopted. Indeed, these measures alongside several weaknesses in government institutional, legal and enforcement measures contributed to the poor development outcomes. This underscores the importance of a strong state capacity for ensuring a more effective implementation of certain prerequisites necessary to facilitate a more significant ‘trickling down’ of benefits to the rest of the Zambian economy, from the privatisation and private ownership of the mines.

In light of the strategic importance of the mines to the Zambian economy and the highly negative consequences in the short term of the privatisation of the copper mining companies on Zambia’s socio-economic development and in increasing the poverty levels, the privatisation option might not have been the best choice for maximising the development of the country. In instances involving strategic activities in a competitive market, SOEs would, in fact, be desirable over private ownership (Cook & Kirkpatrick, 2000a:211, 212). A greater exploration of suitable alternatives to the privatisation option, probably a restructuring through a highly improved management of the ZCCM, possibly within a continued government ownership of the mines, was necessary before the decision to privatise the mines was pursued. Such an arrangement would also require rigorous government oversight to minimise the transfer-pricing policies that characterised the operations of managers under private management and government majority ownership of the mines between 1970 and 1973.

The principal conclusions from this study of the roles of mining TNCs in the mining sector of Zambia are that in the short term within a weak state, the costs of the participation of TNCs in the Zambian mining sector greatly reduced the advantages for the Zambian economy. On the other hand, the capital and technological contributions of mining TNCs to the Zambian economy, at present their most significant contribution to the mining sector, enabled much-needed investment also for recapitalising the mines. However, various factors, together with loopholes in government measures (respectively considered in Section 7.3.1 and 7.3.5), limited the extent of TNCs’ technological and capital contributions to the mining sector.

An assessment of the overall gains for the host country from the participation of mining TNCs requires an evaluation of the benefits of technology and capital inputs from the mining TNCs against the net gains for the Zambian economy from mining surpluses. Poor returns for the government of surpluses from mining severely curtailed the capturing of higher gains for Zambia from the exploitation of mining resources under TNCs' ownership of the mines. The poor returns to the government from mining were mainly due to: (i) low government tax revenue (mainly as a result of excessive concessions granted to mining TNCs); (ii) limited foreign currency earnings to Zambia from copper earnings (largely as a result of transfer pricing policies); and (iii) the weak development of local capacities. In particular, long-term concessions granted to mining TNCs and the repatriation of mining revenue that obstructed the accumulation of higher foreign currency reserves in Zambia greatly limited advantages for the Zambian economy from improved company performance under private ownership. Moreover, the excessive concessions granted to mining TNCs, whilst eliminating subsidies to local companies, created distortions and effectively amounted to a transfer of subsidies from local to foreign capacities and to the government subsidising the operations of TNCs. This constituted a 'dead loss' to the treasury.

In addition, lower gainful employment of the mineworkers, the degrading of the conditions of employment of mineworkers, and the substitution of local capacities to the mines with foreign capacities undermined rather than promoted local capacities. The poor returns to the government from mining through taxes and investment also into alternative non-renewable sectors, such as the development of local workers and suppliers, is the opposite of what is needed for non-renewable resources. These are also inappropriate in light of the short life-spans of some of the mines. Rather, non-renewable resources require the maximising of rent capture by the government to compensate for their depletion or finite income, and employment opportunities and investment into the development of lateral sectors and human capital development and to ensure more sustainable development of the economy (see, for example, Blignaut & Hassan, 2002:89-101; Pedro, 2004:6). The poor returns from mining also precluded a greater diversification of the economy.

This study further found that the concessions and liberal policies were not significant in the locational decisions of mining TNCs that were more fundamentally influenced by other economic factors. In particular, the quality of the minerals and the competitiveness of the country relative to others played a crucial role in the locational decision of companies. The global profit-maximisation decisions of the parent company also strongly influenced Anglo American's decision to leave Zambia.

The limited trickle-down of surpluses from mining to the Zambian economy, and the consequent negative development outcomes from mining under TNCs' ownership of the mines, within a weak state, compared to under government ownership, challenges the neo-classical arguments that ascribe highly beneficial outcomes to host countries from the activities of TNCs. On the other hand, it supports the 'resource curse' argument that resource-abundant economies tend to grow less rapidly than resource-scarce economies. However, the 'curse' was amplified under TNCs' ownership of the mines.

Nonetheless, weak returns and adverse consequences from mining TNCs are not inevitable. Rather, the power asymmetry between the host government and the mining TNCs in favour of the TNCs significantly influenced these outcomes. The poor capacity of the government enabled the TNCs to behave opportunistically and to tip the balance of advantages in their favour. It further contributed to the degrading of the political economic development of the mineworkers and suppliers to the mines, and of the economic development of Zambia. The main factors that contributed to the weak state were the poor performance of the economy, the high external debt and the resultant dependence on IMF/World Bank aid and policies, loopholes in regulation, poor institutional and enforcement capacity, and the concomitant weak bargaining leverage of the government.

These findings highlight the importance of stronger government capacities and certain government measures and interventions to steer the activities of mining TNCs to greater advantages for Zambia. A stronger state capacity also appears pivotal to enable countries to escape the 'curse' of a minerals-based economy. Fundamental blocks for a stronger state capacity, applicable to the mining sector are competent institutions (in particular, economic institutions), a greater corporatist role of the government and effective industrial policies. Effective industrial policies also need to promote efficient and competitive local industries. The liberal policies that the MMD government adopted, however, precluded the development of a greater corporatist role for the government and the adoption of effective industrial policies to encourage the development of local suppliers to the mines. Sustainable economic development also requires a greater diversification of the economy to reduce Zambia's high dependence on copper mining, a non-renewable resource that accounts for the 'Dutch disease' from which Zambia has historically suffered.

Finally, the overall conclusions from this study are that under government ownership of the mines, redistributive measures of mining surpluses in the absence of growth contributed to problems of unsustainability. On the other hand, while growth is necessary for sustainable development, this study demonstrates that it is not by itself a sufficient condition for equitable development. Growth without redistribution, the case under private ownership of the mines, undermined the welfare of Zambians. Sustainable and more equitable development requires both growth and a redistribution of benefits to more disadvantaged sectors of the economy.

The privatisation and the private ownership of the mines by mining TNCs do not have inevitable positive or negative outcomes on the development of the country. However, within a weak state and alongside the liberal policies that the IMF and the World Bank imposed on the MMD government, privatisation and the private ownership of the mines by TNCs failed to generate positive political-economic and development consequences for the host country. On the contrary, within a weak state, opportunistic practices of the private mining TNCs invariably skewed gains in their favour, at the expense of the Zambian economy, the mineworkers and the suppliers of the mines. The concentration of the political-economic benefits from copper mining mainly with the mining TNCs that manifested into increased inequality and poverty levels in the country following the privatisation and the private ownership of the mines by TNCs represents the antithesis of development. Accordingly, the building of a strong state capacity and the institution of fundamental prerequisites before the mines were privatised were crucial for ensuring more advantageous outcomes for Zambia from the privatisation of the mines. These measures were also necessary to steer the activities of mining TNCs to more favourable gains for the country.

Topics for future research

Topics and aspects for future research of the mining sector in Zambia, not addressed in this study, include:

- A study of asymmetric responses in the supply elasticity of copper to changes in copper prices under private and government ownership of the mines.
- A quantitative analysis of the contribution of different factors to the production levels of copper.
- A quantitative analysis of the benefits of private ownership of the mines by mining TNCs and of the costs, especially losses through outflows of surpluses from mining through transfer pricing practices, the repatriation of profits and through huge concessions granted to mining companies.
- A profit-based evaluation of the performance of private mining companies in Zambia.
- An investigation of the development consequences for Zambia of TNCs' ownership of the mines, post the copper price boom of 2004-07.

ANNEXURE

Table A1: Privileges that AAC and RST enjoyed under government majority ownership but under their management control over the mines, 1970-73

During 1970-1973, the management and other powers that the private mining TNCs, AAC and RST, enjoyed enabled them to benefit from:

- Managerial responsibilities that these companies, respectively, enjoyed over NCCM and RCM, for 10 years.
- The 'sole and exclusive rights' over the sales and marketing of minerals and metals, through their parent companies, at a very high fee of 1.5% of the gross turnover, plus 2% of the profits.
- The provision of financial, commercial, technical and other services granted, respectively, to NCCM and RCM, at a considerable consultancy fee of 0.75% of turnover and 2% of profit, after mineral tax but before income tax.
- Recruitment being left entirely in the hands of these minority shareholders, at a high fee.
- The considerable powers of veto that they enjoyed. These included the power to decide on: the winding up of operating companies; the disposal of assets; the granting of mining concessions or other substantial rights to others; enlarging the companies' activities; financial commitments; the borrowing of money; and the appropriation of capital expenditure (also for exploration or prospecting), etc.
- The preferential treatment granted to them in exchange control regulations, permitting the automatic externalisation of non-taxable profits, dividends, management fees and from the sales of the private mining companies.
- The provision in the agreement protecting them against any increases in mineral taxes, export taxes, income taxes, royalty payments, withholding taxes, or any other revenue measures, as long as their bonds (owed to private mining companies for nationalising the mines) were outstanding.
- The permission granted to them to write off all their expenditure, in full, in the year in which they were incurred.[709]
- The formula for the redemption of bonds and the provision in the agreement for a fixed minimum amount of ZIMCO bonds, to be paid each year to these private mining companies,[710] irrespective of the profitability of the mines, and through the acceleration of the redemption of bonds when profits were high. No provision existed for extending the period of these bond redemptions, should the mines experience a sharp decline in their profits.
- Protection against default, by: (i) shielding AAC or RST against the government's defaulting on its ZIMCO bonds; (ii) requiring the government to redeem all outstanding ZIMCO bonds in the event of an unlawful cancellation of management and sales, or marketing contracts by the state; (iii) granting these companies the privilege to appoint the managing directors of RCM and NCCM; and (iv) government assurances not to raise taxes above 73% of company profits.
- Borrowing from external sources a major part of their capital for expansion programmes, rather than employing internal profits.
- Sourcing several services from outside Zambia, despite many of the services having being available in the country.

Sources: Sardanis (2003:268, 269); Saasa (1987:40).

709 Prior to the agreements, the capital expenditure was spread over the life of the mine.
710 To compensate them for the government majority ownership of the mines.

Table A2: Policies of the NERP (1987-88)

The policies of the NERP introduced by the Kaunda government encompassed:

- Suspending part of Zambia's debt payment to the IMF and the World Bank by:
  - Placing a ceiling on the country's debt service payment to 10% of net foreign exchange earnings (but only after essential import requirements were met), estimated to cover only one-sixth of the unrescheduled debts.
  - Suspending interest payments to both the IMF and the World Bank.
- Suspending the foreign exchange auctioning system, which was followed by the government over-inflating the currency and fixing the exchange rate, from 21 May 1987 until 1988, at US$1=ZK8.00, from the previous rate of US$1=ZK21.
- Reintroducing controls in foreign exchange earnings, through allocated foreign exchange control measures, via the Foreign Exchange Management Committee.
- Fixing the interest rates:
  - The interest rate that was 35% during the 1984-86 period was reduced to 15% but with a flexible margin, not to exceed 5% to 20%. This was partly done to assist indigenous firms that had been priced out of the market by the high interest rate policy of the IMF.
- Reintroducing direct price controls through the Price and Incomes Commission:
  - The government nationalised the private maize meal milling companies, and also reintroduced a subsidy on maize meal.
- Setting up a revolving fund facility to support small-scale entrepreneurs, previously bypassed by the IMF policies.
- Establishing an Export-Import Bank to help exporters of non-traditional exports.
- Planning, after a five-year neglect in public investment programmes, to expand public works schemes in rural areas, to stimulate employment opportunities and to expand its future revenue base.
- Reaffirming its support for collective bargaining.

Sources: Cherv (1989:133, 138, 139); Hanson and Hentz (1999:484); Lungu and Silengo (1997:15); McGrath and Whiteside (1989:172, 176, 178, 179); Simutanyi (1996:827); The Economist Intelligence Unit (2002:5); ZCTU File (cited in Akwetey, 1994:56).

Table A3: Different structural adjustment policies that the Kaunda government adopted in the 1980s

1983	June 1984	October 1985	1989-93 (the policies extended two years into Chiluba's government)
1st SAPs adopted, which was a fundamental policy shift from previous attempts at economic reform. Zambia was granted a credit of SDR 270 million The policy reforms broadly included: • Fiscal and budgetary reforms to: o Restore financial discipline o Improve the government's debts servicing capacity, through demand management • A diversification of the economy to agriculture that was to be funded through copper revenues More specific major objectives of the 1983 agreements included: • A devaluation of the currency by 20%[711] • A restriction of wage increases to 5% • The decontrol of prices of essential commodities and • The removal of subsidies on maize and fertilisers	Zambia adopted a new standby agreement with the IMF for SDR 225 million. However, only SDR 85 million was drawn, as a sudden fall in the price of copper prevented the government from servicing its arrears of about US$800 million	A very comprehensive economic adjustment programme was adopted, including: • Most of the measures adopted in 1983 • Demand-side measures: o Cuts in government expenditures (including the closure of three mines o Reductions in civil service employment o Freezing of wages o Removal of subsidies o Eliminating new investments in public projects • Supply-side measures o A foreign exchange auction system was central to the programme (introduced in October 1985) and was aimed at streamlining the allocation of foreign exchange o Pricing policy ▪ Most of the prices of consumer goods, apart from maize, were decontrolled ▪ The import licensing system was eliminated	The strategy of the SAPs of 1989, set out in the PFP of 1989-93, included: • A deregulation of all price controls and a market determination of all consumer prices, with the exception of maize, maize meal[712] and fertiliser • Changes in the exchange rate system: o The currency was depreciated by 50% in 1989 o The introduction in 1989 of a dual exchange rate allocation system with two windows[713] o A market exchange rate was introduced in 1990, with the deregulation of the foreign exchange o A unification in 1991 of the official rate and the market exchange rate • A more open trade regime was encouraged through: o The cutting of the maximum tariff rate from 100% to 50% in 1990 and to 40% in 1993 o Reductions in the tariff bands in 1993 from 6 to 4

[711] That led to a sharp increase in interest rates.
[712] A coupon system was introduced for the purchasing of maize meal, to soften the impact of the SAPs on the poorer sections of the population.
[713] At the first window, foreign exchange earnings were sold to copper-related importers and importers of oil and of fertiliser, while foreign exchange at depreciated rates was sold at the second window for the use of others (Lungu and Silengo, 1997:15).

1983	June 1984	October 1985	1989-93 (the policies extended two years into Chiluba's government)
Zambia's failure to pay its overdue debt to the IMF of SDR 75 million and to meet its budgetary targets led to a suspension of the 1983 Standby Agreement, in June 1984, with SDR 67 million undrawn		○ Decontrol of interest rates ○ Reform of the public sector to improve efficiency • The liberalisation of the agricultural market	• The raising of the reserve requirements of the banks, which reduced funds for lending of the commercial banking sector • The raising of interest rates from 18% to 42% that greatly discouraged borrowing

Sources: Africa Now, June (1987:31); Cherv (1984:132, 136; 1989:131, 132); Lungu and Silengo (1997:14, 15, 16); Simutanyi (1996:826, 827); McGrath and Whiteside (1989:172); World Bank (2002b:28).

Table A4: Stabilisation and adjustment policies that the Chiluba government adopted

- Price decontrols of all products (except maize) and inputs
  - Price controls on all products and inputs were dismantled by early 1993, save for a policy of restraint on wages
  - By the end of 1993 all subsidies on maize meal and fertilisers had been withdrawn that led to a dramatic increase in the price of maize meal from K250 to K4 000 in November 1991

- Exchange rate adjustments in real terms and the elimination of exchange rate restrictions
  - The liberalisation of the foreign exchange, following the unification of the previously dual exchange rate in 1993, was partly achieved through the introduction of the Bureaux de Change
  - The Exchange Control Act was abolished in 1994. Zambia has some of the most liberal banking regulations in Southern Africa

- Monetary policy measures to adjust interest rates and to tighten monetary policy
  - The objective of monetary policy was to reduce and contain levels of inflation and to maintain money supply at levels consistent with the desired economic growth
  - The borrowing and lending interest rates were decontrolled in October 1992, with the elimination of all interventions in credit allocations and in interest rates, following the establishment of the Treasury Bill Auction
  - The Treasury Bill Auction, as a less inflationary form of public borrowing, however, led to a substantial rise in the nominal interest rate and the real rate has been positive for most of the time
  - Public revenue was increased through mechanisms such as user charges and a semi-autonomous revenue service

- The liberalisation of export and import trade, while providing export incentives
  - Product and factor markets (excluding land) were liberalised
  - Trade liberalisation was introduced by the end of 1995, facilitated through:
    - Simplifying the tariff structure, by further reducing the maximum tariff rate from 100% to 40% in 1993 (although a temporary 5% import levy was introduced across the board in October 1995 to meet revenue needs). By 2002 the average tariff rate was about 10% and the maximum tariff rate was 25%
    - Reducing the number of tariff bands in 1996 from 6 to 4 (namely, 0%, 5%, 15% and 25%)
    - The elimination of tariff exemptions. This was partly achieved through a progressive increase in the Common Market for Eastern and Southern Africa (COMESA) tariff preference, to a minimum of 40% of the corresponding rate for general imports
    - Abolishing, in July 1995, the 20% uplift factor on duties that applied to import values
    - The elimination of import sales tax in 1995
    - Removing quantitative restrictions on imports and exports
  - A more outward-oriented trade regime was favoured through export incentives
    - Non-tariff barriers (NTBs) and export bans and taxes were eliminated in 1991, with the ban on the export of maize being lifted in 1993 (although temporarily reinstated in mid-1995)
    - A system of export incentives (duty drawback, manufactures-under-bond) was introduce
    - An Export Promotion Board was set up

- Fiscal austerity measures to reduce the budget deficit and to control inflation
  - Fiscal austerity measures to reduce the public budget deficit would be implemented and were aimed at curbing public expenditure

- The reform of the civil service and parastatals to improve efficiency and performance

This was to be achieved through:

- Huge retrenchments of public sector workers
- The reconstitution of public expenditures to phase out subsidies
- Reductions on social expenditure and on bureaucracies
- The control of inflation

- The reform of the public investment programmes to focus on resource allocation to priority sectors and programmes

- The privatisation programme
  - State assets were privatised and some state enterprises were liquidated

Sources: Bank of Zambia (2003:5); Craig (2002:2); MUZ (1994:3); Simutanyi (1996:828, 829); The Economist Intelligence Unit (2002:29, 44); Tshoedi (2000:86); World Bank (1996:11, 2002a:18, 2002b:28) and interview with Silane Mwenechanya, 24 October 2003.

Table A5: Summary of the main transactions in the privatisation of the ZCCM

Date of agreement	Assets	Buyer	Principal terms of sale	Name of new company
January 1997	Kansanshi Mine Package "E"	Cyprus Amax Minerals Company (USA)	• Cash US$3 million • Conditional cash up to US$25 million • Committed investment US$20 million • The ZCCM retained interest 20%	Cyprus Amax Kansanshi plc changed to Kansanshi plc
		Phelps Dodge took over from Cyprus Amax for 1 year		
1999		First Quantum took over from Phelps Dodge in 1999 Ownership in 2001: • First Quantum – 80% • ZCCM-IH – 20%	First Quantum paid US$25 million for the Kansanshi mine	
June 1997	Luanshya Division Package "B"	RMC Trading (Irish): Comprises of: • Binani Industries (India) • Dallah Albaraka Bank (Saudi) • Ispat International (owned by Lakshmi Mittal) Ownership • Each of the above companies had equal ownership, amounting to a total of 85% and • ZCCM-IH – 15% Ownership of RAMCOZ changed, however, with it being placed under receivership in November 2000	• Cash US$35 million • Committed investment US$69 million • The ZCCM retained interest 15%	Roan Antelope Mining Corporation of Zambia plc (RAMCOZ)
2004		J and W Investment Group, a subsidiary of Enya (Switzerland) took over from RMC Ownership changed to: • Enya – 85% • ZCCM-IH – 15%	• J and W intends to close down Luanshya Mine and keep only Baluba • The company intends to retain only 1 000 employees and expects the government to pay the retrenchment packages and indebtedness of the laid-off workers	Luanshya Copper Mines (LCM)

Date of agreement	Assets	Buyer	Principal terms of sale	Name of new company
			• Demands more concessions than KCM did	
October 1997	Chibuluma Mine Package "A"	Consortium consisting of: • Crew Development Corporation (Canada) • Maranda Mines (South Africa) • Genbel Securities (South Africa) Ownership before 2003: • Metorex Consortium – 85% • ZCCM-IH – 15%	• Cash US$17.5 million • No deferred payment • Committed investment US$34 million • Conditional copper and cobalt price participation of US$7.6 million[714] • Accepted no liabilities, except for terminal benefits of employees • The ZCCM retained interest of 15% (all free carry)	Chibuluma Mines plc
		Ownership in late 2003: With IDC's (South Africa) involvement in Chibuluma South the ownership changed to: • Metorex – 80% • ZCCM-IH – 9.78% • IDC – 10.2% Metorex bought a new copper licence to reopen its Chibuluma South Mine Ownership of Chibuluma South: • Chibuluma Mines – 65% • IDC – 35%		
November 1997	Power Division Package "J"	CEC comprised of: • Midland Power International (UK) • National Grid (UK) • Synergy Global Power (USA) • Zambian managers (five senior managers) Ownership: • Synergy – 38.5% • National Grid –38.5% • ZCCM-IH – 20%	• Cash US$50 million at close • Conditional deferred cash US$7.5 million[715] • Unconditional debt assumption US$73 million • Committed investment US$25.5 million • Conditional debt	Copperbelt Energy Corporation plc (CEC)

714 Copper price participation level was at US$l/lb, amounting to US$1.2 million, and cobalt contribution of 40% at US$15 a pound, amounted to US$6.4 million.
715 Contingent upon signing a long-term power agreement for KDMP (Kaunda, 2002: 175, 176).

Date of agreement	Assets	Buyer	Principal terms of sale	Name of new company
		• Five Zambian managers – 3%	assumption US$61 million[716] • Contingent capital expenditure US$60 million over 15 years • An employee share ownership was to be made available also to employees other than senior managers • The ZCCM retained interests 20%	
June 1998	Chambishi Mine Package "D"	China Non-Ferrous Metal Industries (China) Ownership: • NFCA – 85% • ZCCM – 15%	• Cash US$20 million • Committed investment US$70 million • Employee-accrued terminal benefits taken over by buyer • The ZCCM retained interests 15%	NFCA Mining plc
September 1998	• Chambishi Cobalt and Acid Plant Package "G" and • Nkana Slag Dumps Package "A"	Anglovaal Ltd (AVMIN)(South Africa) Ownership: • AVMIN – 90% • ZCCM-IH – 10% Ownership changed to: • AVMIN – 55% • Anglo – 35% • ZCCM-IH – 10% Anglo, however, sold its shares back to AVMIN, following its decision to withdraw from KCM	• Cash US$50 million • Conditional cash up to US$45 million, conditional on future cobalt prices[717] • Committed investment US$70 million • Employee accrued terminal benefits taken over by buyer • The ZCCM retained interest 10% (5% free and 5% interest repayable carried)	Chambishi Metals plc
2004		J and W Investment Group, a subsidiary of Enya (Switzerland) took over ownership of Chambishi Metals from AVMIN Ownership changed to: • Enya – 90% • ZCCM-IH – 10%	J and W paid AVMIN an amount that net the liabilities and the assets	Chambishi Metals
September 1998-2000 after which Binani left	Ndola Precious Metals Plant	Binani Industries (India) Ownership: Binani – 100%	• Cash US$0.35 million • Deferred cash US$0.18 million • Conditional cash up	Minerva (PMP) Limited

716 Contingent upon achieving higher demand forecasts (Kaunda, 2002:176).
717 Over a period of about five years (ZCCM, 1999:8).

Date of agreement	Assets	Buyer	Principal terms of sale	Name of new company
			to US$0.8 million	
31 March 2000	• Mufulira Division (Package "C") ○ Underground mine ○ Concentrator ○ Metal treatment assets comprising of: ▪ smelter[718] ▪ refinery[719] • Nkana Assets (Package "A")** ○ Mines ○ Concentrator Cobalt Plant	Buyers comprised of: • Glencore International (Switzerland) • First Quantum Minerals (Canada) Ownership before 19 April 2002: • Glencore International – 46% • First Quantum Minerals – 44% • ZCCM-IH – 10% Ownership after 19th April 2002720 changed to: • Glencore International – 73.1% • First Quantum Minerals – 16.9% • ZCCM-IH – 10%	• Cash US$20 million • Deferred cash up to US$23 million, conditional on future copper prices, payable in five equal instalments of US$4.6 million, commencing on 1 January 2003[721] • Committed investment US$159 million[722] within 3 years following close • Conditional investments of about US$343 million,[723] while that for Nkana remained unchanged, subject to further evaluation of the assets • Upwards adjustment of the ZCCM's payment by copper price participation on a pro-rata monthly basis, calculated at 2% for every US$0.01 of the copper price, over and above US$0.85/lb, payable for five years from 2003 and capped at US$4.4 million. Payments were to be capped at US$9 million per annum • Employee accrued terminal benefits taken over by buyer • Glencore was to provide Mopani with a 3-yr revolving	Mopani Copper Mines plc (MCM)

718 Most cost-effective of Zambia's three smelters.
719 Most efficient of the three refineries available in Zambia, which include Luanshya and Nkana.
720 Following heavy losses at MCM in 2001.
721 The first instalments were, however, not paid by 2003 (interviews with Emmanuel Mutati, 18 November 2003 and Chuma Kabaghe, 18 November 2003).
722 US$75 million for the operations of Nkana and US$84 million for Mufulira.
723 US$103 million for operations at Mufulira and US$240 million for operations at Nkana.

Date of agreement	Assets	Buyer	Principal terms of sale	Name of new company
			US$25 million working capital facility at LIBOR+3% and an additional US$15 million standby working capital facility • The ZCCM retained interests 10% (5% of which will be free carried interest and the other 5% will be repayable carried interest)	
March 2000-2002 after which the Anglo led consortium left	• Nchanga Division[724] (Package "A") comprising of: ○ An open pit and an underground mine ○ Nampundwe Pyrite Mine[725] (Package "F"); ○ Chingola Refractory Ores (Package "L"); ○ Infrastructure associated with the above (including Konkola, Nchanga, Nampundwe Concentrators and Nchanga	Anglo American led consortium comprising of: • ZCI,[727] a subsidiary of Anglo American[728] (Anglo American invested indirectly in KCM, through ZCI in which it had 51% equity interest and 49% of ZCI is owned by market investors). Since ZCI, in turn, owns 65% of KCM the shareholding attributable to Anglo in KCM was 33%, which made Anglo the largest individual shareholder • IFC[729] • CDC[730]	• Cash US$30 million • Deferred cash payment US$60 million, payable in six annual instalments, starting from 1 January 2006[731] • US$125 million conditional on copper and cobalt price participation[732] • Committed investment[733] for existing operations US$208 million • Committed investment for Konkola Deep US$523 million[734] • Anglo American sold	Konkola Copper Mines plc

724 Comprising of an open pit that commenced operations in 1957, an underground mine that started operation in 1937, a concentrator and a tailings leach plant. It was ZCCM's largest copper and cobalt producer and is the most productive mine on the Copperbelt, but by 2003 it had only six to eight productive ore years left (The Economist Intelligence Unit Limited, 2002:40; Kaunda, 2002:81).

725 Nampundwe Mine, which started operations in 1970, produces pyrite concentrate used for the production of sulphuric acid at Nkana Mine and at the fertiliser plant Nitrogen Chemicals of Zambia (Kaunda, 2002:81). Anglo bought the Nampundwe mine that had little value mainly to utilise pyrite at this mine for the production of sulphuric acid used at Nchanga's Tailings Leach Plant (Kaunda, 2002:186).

726 That was Anglo's main interest to develop and exploit (Kaunda, 2002:186).

727 ZCI is listed on the JSE Securities Exchange South Africa, the London Stock Exchange plc and the Paris Bourse (Times of Zambia, 2002:2).

728 The merger of Minorco SA and Anglo American Corporation in October 1998 formed Anglo American plc, which became one of the world's largest mining and natural resources companies (ZPA, 2000c:39).

729 Arm of the World Bank.

730 The CDC.

731 Interview with L. M. Lishomwa, 29 October 2003.

732 This amount is to apply over the life of the assets and is subject to a maximum payment in any year of US$16 million (ZPA, 2000c:38 and ZPA, 2000d:152).

733 For existing Konkola and Nchanga operations within three years following close (Kaunda, 2002:89).

Date of agreement	Assets	Buyer	Principal terms of sale	Name of new company
	tailings leach plant) ** • Konkola Division that includes: o Nchanga Smelter o Refinery o Acid plant o KDMP, a large underground copper-rich ore body below the current mining level at the Konkola Division[726]	Ownership before Anglo's withdrawal: • ZCI – 65% • IFC – 7.5% • CDC – 7.5% • ZCCM-IH – 20% Ownership after Anglo's departure before Vedanta Resources took over: • ZCCM-IH – 42% • ZCI Holdings (SA) – 58%	its 27.3% stake in the ZCCM to the Zambian government for US$30 million in cash; the payment was to be effected in 8 annual instalments, commencing on 1 January 2006 • Employee accrued terminal benefits to be taken over by the buyer • Costs of retrenchments of mineworkers to be paid by the government with the assistance of the World Bank that contributed over US$65 million as a loan • Various tax breaks • Anglo ruled out taking on any of the ZCCM-funded local schools and hospitals • The ZCCM retained interest 20% (5% free:15% carried)	
End 2004		Vedanta Resources, a company of Sterlite Industry (British/Indian) took over ownership from Anglo, CDC and IFC Ownership end-2004 • Vedanta Resources – 79% • ZCCM-IH – 21%	• Cash US$48.2 million	

** Denotes that both agreements also included options relating to parts of the Nkana Division processing plant.

Sources: Africa Mining Intelligence (2002c:1, 2002d, 2006a:3); Africa Research Bulletin (2000a:14302); Craig (2002:368); Engineering and Mining Journal (2000a:36, 2000b:11, 2000c:26); Fraser and Lungu (2007:13); Metals Place (2007); Regional Investor Survey (2001:38); Kaunda (2002:16, 46, 72, 82, 88, 89, 90, 111, 116, 175, 176); The Economist Intelligence Unit (2002:40, 41, 42; 2007b:35); World Bank (2002a:26, 2003b:132); Zambia Daily Mail (2002:5); ZCCM (1999:8, 2000:7, 8); ZPA (2000c:33, 37, 38, 39; 2000d:127; 2002:33) and interviews with Simon Capper, 30 October 2003; Andrew Hickman, 7 November 2003; Silane Mwenechanya, 24 October 2003; Thomas Kabandama, 13 November 2003; Gary

[734] Commencement of the implementation of KDMP was to start 18 months after close, provided that long-term limited recourse project finance was available from third party lenders on reasonable commercial terms. The investment was not to be internally generated by KCM but by ZCI and any parties selected by them (Kaunda, 2002:89).

Loop, 29 October 2003; Chama Kapambwe, 11 November 2003; L. M. Lishomwa, 29 October 2003; Emmanuel Mutati, 18 November 2003 and Chuma Kabaghe, 18 November 2003.

Table A6: Factors that reduced the bargaining leverage of the government at the time that the mines were privatised

(a) <u>The poor economic position of the ZCCM and of the Zambian economy:</u>

- The ZCCM experienced great financial losses immediately before KCM and MCM were privatised:
  - The huge financial losses and accumulated arrears that the mines incurred threatened the ZCCM with possible bankruptcy. Privatisation was therefore a 'damage control exercise', partly to relieve the national budget from covering the losses of the mines, according to the World Bank.
    - Losses of the ZCCM increased from a net loss of K198 722 million in the 1996-97 financial year (ending 31 March 1997) to a net loss of K260 385 million in the 1998-99 financial year. This was however an improvement on the loss of K604 028 million registered in the 1997 financial year. The net losses were exacerbated in the financial year ending 31 March 2000, at K807 470 million. Accordingly, the average operating losses were US$935 million from 1997 to 2001, amounting to an average of over US$15 million per month.[735] However, the ZCCM continued to operate until the mines were privatised but immediately prior to its privatisation focused mainly on short-term returns and on saving the ZCCM from possible collapse.
    - The losses to the economy had an adverse impact on Zambia's:
      - Current-account balance, as a result of declines in the country's foreign exchange consequent to the drop in copper production.[736]
      - Debt.
- High government debt before the ZCCM was privatised lowered its bargaining leverage. The high debt was mainly owing to:
  - The enormous external debt of the country of US$7 billion in 1996. In 2000, the debt of the government comprised of: (a) US$273 million to suppliers, including about US$100 million owed to ZESCO; (b) US$298 million to the Paris Club; and (c) US$195 million to multilateral agencies. These debts of the government amounted to about US$770 million in 2000 that became a significant burden for the government, especially in light of the balance of payment difficulties that the country experienced.
  - The government's assumption of the liabilities of the ZCCM that added about US$300 million to the domestic debt immediately before the ZCCM was privatised. The external loan portfolio of the ZCCM stood at US$436 million in May 1998.
    - Government guarantees required for expensive external short-term loans that the ZCCM and other bodies[737] were forced to resort to, as bankers were reluctant to lend to the loss making ZCCM, further raised the debt burden of the government. The government had to pay over US$30 million for the old ZCCM debt and US$20 million for cleaning up the ZNCB portfolio in 2002.
  - Difficulties the Zambian government experienced in keeping up with servicing its international loans, partly due to loans being used to cover losses at the ZCCM.
  - The government being forced to pay the miners' monthly wage bill from its general revenue accounts, just prior to the sale of the remaining assets of the ZCCM.
- The lack of recapitalisation of the ZCCM signified the most significant constraint on the mining sector,[738] according to research conducted by Kapika *et al.* (1996:8). About US$100 million was required to manage the transition until buyers were found.
  - The lack of recapitalisation was largely due to:
    - A shortage of capital, partly as a result of the decline in the copper price in the late 1990s and the lack of significant inflows of funds for capital expenditure, except for recurrent expenditure to merely sustain the mines.
      - The poor credit profile of the ZCCM, and those of the country, especially owing to the

[735] The Chairman of ZACCI and ZPA experts put the figure at $2 million per day, especially just before core assets of the ZCCM were privatised, in March 2000.

[736] From about 321 000 tons in 1997 to only 226 000 tons in 1999.

[737] Including Development Bank of Zambia (DBZ), ZANACO and ZESCO.

[738] Technology and skills from the private sector that was locally available was of less importance than the injection of finance in the privatisation drive (interview with Francis Kaunda, 20 October 2003).

high debt of the ZCCM and the government's enormous external debt, prevented the ZCCM from borrowing US$0.5 billion in 1995 required for investment into the mines.[739] By March 1996, the ZCCM required an injection of about US$2 billion to avoid a complete collapse, which local sources were unable to provide.

            - The private shareholders were unwilling to put cash into the ZCCM.
            - The operations of the ZCCM were sustained through short-term borrowings from local and foreign financial institutions.
        - Government policies to redistribute much of the revenue from copper mining to develop non-mining sectors and to address electoral-maximising concerns.[740]
        - The significant decline in the real value of the world copper price, over the last 20 years.
    - The lack of reinvestment of the ZCCM contributed to:
        - Accelerating the aging and degrading of mining machinery, rendering them inefficient and unreliable.[741]
        - Destroying the internal culture of the mining sector, which proved highly disruptive.
        - Limiting improvements in capacity building through investments in more efficient mining, underground mines, the development of new mines, and through ventures into prospecting and exploration activities. New mining methods were required to extract ore from the thin, irregular and deep-seated ore bodies and to improve recoveries, especially as the grades of ore began to dwindle. Under-investment in exploration and in developing the mining sector led to the need for huge capital investments, of about US$0.5 billion, by 1995/96, to revitalise the existing mines and to open up new mines.
        - A decline in the value of the mines as the ZCCM's assets deteriorated.
        - The fall in the production and productivity levels of the ZCCM, especially after the mid-1990s.
        - A decrease in mining revenue, largely as production levels declined.
        - An increase in the costs of production.
            - The high costs of production, in excess of US$1.0 per pound of copper for most of the mines of the ZCCM, with Konkola experiencing unit costs of US$1.2 per pound of copper, rendered the ZCCM uncompetitive, inefficient and unprofitable.
        - A significant lowering of the global competitiveness of Zambia, as a result of diminished production levels and the increases in the costs of production. Zambian mining fell to the 95th percentile on the world's copper production cost curve in 1995, mainly due to the relatively high fixed costs (labour and other fixed costs) and higher costs associated with deeper level mining. About 70% of the ZCCM's copper came from underground sources.
- The acute decline in the foreign exchange earnings of Zambia contributing to the near collapse of the Zambian economy in the late 1990s:
    - The drop in the foreign exchange earnings was largely due to the increase in the cost of production of copper, alongside the drop in the production of copper and cobalt.
    - A substandard practice within the ZCCM, immediately prior to the privatisation of the mines, to mix waste with ores into the concentrator, which reduced the grade value of copper of 4% by up to 50% after extraction, caused a serious problem of dilution of ores, lowering Zambia's revenue from mining.
    - While export earnings averaged about US$1.2 billion in the 1980s, it dropped on average to

[739] A lack of skills and of technology did not constitute significant factors in the poor performance of ZCCM (interview with Simon Capper, 30 October 2003).

[740] That contributed, among others, to the mines being overmanned during Kaunda's government, but the number of mineworkers was significantly reduced during Chiluba's government (interviews with Andrew Hickman, 7 November 2003; Dennis Wood, 21 October 2003 and Silane Mwenechanya, 24 October 2003).

[741] For example, the Nkana Smelter technology, which by 1996 was one of the most critical plants in the production of copper in Zambia, was over three decades old. Moreover, Nchanga Open Pit, which was the largest copper producer in the ZCCM, experienced a shortage of basic inputs, such as shovels and trucks and the available machinery was unreliable and circumspect.

[742] Such as chemicals, reagents, pump spares, machinery and equipment, for example, mill rods, refractories and loco spares and safety inputs.

[743] For instance, the Credit Guarantee Insurance Corporation (CGIC) of South Africa prevented all its clients from exporting to the ZCCM, while demanding full settlements of long overdue payments before restoration of insurance covers and permission to export.

[744] This demonstrates the non-independence of advisors, according to Francis Kaunda (2002:28).

[745] The demand was likely to discourage the government from making counter-proposals and favoured the buyers, according to Kaunda (2002:29). The request was, though, rejected on an understanding that the liquidation of the ZCCM would likely have culminated in serious political and social instability in Zambia (Kaunda, 2002:28 & 29; Craig, 2001:406).

[746] Donors were rather uncritical of these tactics, according to Kaunda (2002:78).

only US$1 045 million in the 1990s. An amount of about US$3 billion per annum in foreign exchange was required in 2003, to enable the industries in Zambia to operate at full capacity.
  - The donors withheld balance of payments support in 1998, before the KCM and MCM were privatised, forcing the Zambian government to use about US$237 million of its reserves. This left the country with a residual reserve of only US$9 million towards the end of 1998. In 1999, the ZCCM sold less than US$20 million in foreign exchange to the BoZ, owing to its poor performance.
  - The shortage of foreign exchange in the mining sector was also transmitted to the manufacturing sector and to industries that imported raw materials.
- The tax revenue of the ZRA and the customs revenues declined as the economy shrank.

(b) Pressure from suppliers and shortages of supplies

- Stringent demands from local and in particular foreign suppliers of mining inputs in 1998 that the ZCCM settle outstanding payment in arrears of up to six months and for upfront cash payment before further spares were to be supplied to the ZCCM severely restricted access to critical production inputs,[742] to the ZCCM. Many resorted to embargoes and litigation threats to limit their financial risks.[743]
- The accumulated arrears of the ZCCM to its Zambian suppliers of goods and services prompted Zambian suppliers' demand for a swifter privatisation of the ZCCM.

(c) Pressure from donors and from foreign actors:

- The linking, shortly before the Paris Club meeting, of the conclusion of the privatisation of the remaining mining assets of the ZCCM (that was also made a benchmark for the debt relief programme), on the release of US$530 million in donor balance-of payment support, pledged in May 1998, proved decisive in hastening the privatisation of the ZCCM.
- Foreign Advisors, Rothschild and Clifford Chance pressurised the government, by tabling a resolution for the voluntary liquidation of the ZCCM,[744] on 28 February 1997, at the same time the first bids were received, which threatened the company with collapse.[745]
- Allegations exist that foreign advisors also divulged information regarding the value of the mines to the Kafue Consortium, further lowering the government's bargaining leverage.

(d) Unfavourable external factors:

- The declines in copper and cobalt prices on the international market (especially in 1998), lowered the investment attraction of copper and the likelihood of the ZCCM becoming a viable concern.
- The volatile political climate in some neighbouring countries created uncertainty as to the foreign investment prospects in Zambia.

(e) Certain strategies that the TNCs employed and factors that increased their bargaining leverage:

- Strategies that TNCs employed and factors that increased their bargaining leverage over those of the government included:
  - Anglo American's knowledge of the ZCCM's poor economic status (enabled through its position as a shareholder on the board of that company); the pressure of a time limit within which the Zambian government had to privatise the ZCCM and; the possibility that the government would otherwise forfeit balance of payments support from donors.
  - The strengthening of the bargaining leverage of the Kafue Consortium, through donors linking the completion of the ZCCM's privatisation (specifically the disposal of Package 'A'), to further balance of payments support. This encouraged the Kafue Consortium bidders to harden their stance and to make significant demands just before Consultative Group meetings with donors.[746] The Kafue Consortium flexed its muscles partly through a walkout in the London meeting, on 14 April 1997, following a request from the Negotiating Team for further changes to their bid and for clarification on the reduction of their first bid by US$100 million, within only one and half months of the initial bid.
  - The pre-emptive rights that Anglo American enjoyed over the sales and some mining activities that increased its bargaining leverage above those of other mining companies.
  - Anglo American being the sole bidder for the 'Aco' package that, in the context where the government was pressurised to privatise the ZCCM within a certain timeframe, left it

vulnerable to accept the mining company's offer.

- The possible threat that TNCs could locate elsewhere, because of their ability to shift resources to other countries.
- Possible collusions by some mining TNCs in the bidding process, through the formation of consortiums and through the cross-sharing of ownership, which, the Third World has great difficulty in dissecting.
- Foreign mining companies exaggerating the poor state of the mines to obtain more concessions from the government.
- The huge investment benefits that the TNCs pledged for the Zambian mines, especially the Konkola Deep Mines, encouraging the government to concede to many of the concessions demanded from Anglo American.

Sources: Bull, cited in Profit Magazine (1998:128, 129); Business in Africa (2002:2); Craig (2001:405, 406); Committee on Economic Affairs and Labour (2000:47, 48, 49, 58); Kaunda (2002:24, 34, 35, 37, 60, 149, 162); Kapika et al. (1996:6, 7); Ministry of Finance and Economic Development (1996:57); Maambo (1998:Fig. 7); New York Post (1998:1); SADC (2000:340); The Economist Intelligence Unit (2002:29); Transparency International (2002:17); Van Buren (2003:1152, 1155); World Bank (2002a:14; 2002b:1, 7, 14, 15, 17, 24; 2003b:131, 132, 133); ZCCM (1996:6;1997:22; 1998:38;1999:6, 11; 2000:5, 10, 11); ZPA (2000b:14, 2000c:34) and interviews with Emmanuel Mutati, 18 November 2003; Stuart Cruickshank, 28 October 2003; Fortune Kamusaki, 25 November 2003; Honourable Dipak Patel, 15 October 2003; Ladslous Mwansa, 7 October 2003; Ohene Nyanin, 29 November 2003; Jack Jones, 22 October 2003; Honourable Eugene Appel, 24 November 2003; M. Shandavu, 10 October 2003; Andygean Luombe, 8 October 2003; Zion Simwanza, 1 December 2003; Francis Kaunda, 20 October 2003; Valentine Chitalu, 22 October 2003; Silane Mwenechanya, 24 October 2003; Chama Kapambwe, 11 November 2003; Wilphred Katoto, 12 November 2003; Alick Lungu, 14 October 2003; Honourable Captain Moono, 2 December 2003; David Chilipamushi, 20 October 2003; Willie Sweta, 30 October 2003; Sipho Phiri, 30 October 2003; Dennis Wood, 21 October 2003; Simon Capper, 30 October 2003; John Lungu, 12 November 2003; Fred M'muembe, 14 October 2003; Andrew Sardanis, 19 October 2003; Charles Muchimba, 18 November 2003; Danny Kalyalya, 31 October 2003; Gilbert Temba, 13 October 2003, Thomas Kabandama, 13 November 2003; Dave Phiri, 23 October 2003; Andrew Hickman, 7 November 2003; Kasote Singogo, 16 October 2003; Fred Yamba, 25 November 2003 and Isaac Masonda, 11 November 2003.

Table A7: Factors that undermined the capacity of local industries and suppliers in the mining sector

Major factors and policies prior to and subsequent to the privatisation of the mines that undermined more effective participation of local industries and suppliers in the mining sector during Chiluba's government included:

- The introduction of liberalisation policies in Zambia, before the mines were privatised, which led to the bankruptcy of many local suppliers. Several others had to downsize in order to survive. The closing down of many industries lowered employment in these sectors. In particular:
  - The immense competition from more competitive, lower-cost foreign manufacturers as a result of trade liberalisation policies proved particularly harmful to the manufacturing companies in Zambia.[747] For instance:
    - The increased influx of goods into Zambia, especially from South Africa and from Zimbabwe (that are under-reported, as official figures are likely to capture less than half the total), assisted by Zimbabwe's dual exchange rates, caused the closures of several major operations in Zambia.
    - The range of global and regional free trade agreements to which Zambia is bound, such as the COMESA,[748] which came into force on 8 December 1994, limiting the use of tariffs and quotas to manage the flows of goods, services and capital, undermined the manufacturing sector in Zambia. Moreover, the Free Trade Area (FTA) that would be applicable to the Southern African Development Community (SADC) that would also promote duty free trade would further intensify regional competition.
  - The liberalisation of the financial markets and the foreign exchange market that, respectively, increased the interest rates and the inflation of Zambia raised the production costs of locally-based manufacturing companies (discussed below).
- The absence of an industrial policy and of laws to protect and support local suppliers, while promoting foreign investor-friendly policies.
  - The government failed to provide appropriate safety nets to limit negative consequences of trade liberalisation to local suppliers to the mines and the manufacturing industry in Zambia.
  - The lack of active government intervention, partly through strategic incentives to help local industries surpass the infant industry stage, before trade liberalisation policies were introduced, severely limited their chances to withstand fierce competition from foreign industries.
  - The absence of greater government participation in the development of the manufacturing sector in Zambia under MMD rule, discouraged higher growth in the local manufacturing sector. Alliances with local entrepreneurs were crucial in the building of local capacities and accounted, considerably, for the successful development of the IT industries in India, Brazil and South Korea and which, in turn, attracted TNCs.
  - Increases in import duties on raw materials for manufacturing in the 1990s, over finished goods, which enjoyed substantial reductions in customs duties[749] (the main trade policy instrument employed by the Chiluba government, instead of import controls, which were maintained only for health, security and associated reasons), discouraged manufacturing in Zambia. Conversely, these policies encouraged many Zambian-based companies to switch from the local production of mining inputs to the trading of cheaper imported finished products, mainly consumption products, which flooded the Zambian market after the introduction of trade liberalisation policies.
  - Granting new foreign investors broad incentives,[750] such as duty exemptions on imported equipment[751] and tax exemptions,[752] not extended to existing local companies, while

[747] For example, the expiry of the Agreement on Textiles and Clothing, in 2005, encouraged imports from especially Asian countries that constrained greater growth, mainly in the textile and clothing manufacturing sector (The Economist Intelligence Unit, 2008a:6).

[748] The successor organisation to the regional Preferential Trading Area (PTA).

[749] That enjoys a maximum tariff of 25%.

[750] Provided in the Investment Act of 1991 and through the Investment Centre.

[751] For example, new foreign investors are, generally, exempted from paying import duties on motor vehicles, motorcycles and bicycle assembly plant machinery for the first five years of operating in Zambia. In this instance, though, the policy benefited Zambia, as it secured the establishment of a motor vehicle industry, by Tata, of India in Zambia (Africa Confidential, 2006:4).

removing subsidies previously granted to Zambian companies. The new Investment Act of 2006 is however likely to improve the benefits to local businesses.
    - Zambian manufacturers received no export incentives.
    - Zambia still lacks an industrial policy to attract and encourage forward linkages to the mining sector. Policies and factors that inhibit the development of forward linkages entail:
        - A failure to introduce higher export duties on copper concentrates to encourage the development of local processing industries.
        - High charges for the treatment of copper concentrates in Zambia and the reluctance of local smelters to process the concentrates of some companies including those of Chambishi Metals, forcing the company to export its concentrates to Namibia.
        - The absence of an industrial strategy to encourage forward linkages of mining in Zambia, also other than smelting (where most of the forward linkages of mining at present are concentrated),[753] in which Zambia has a comparative advantage, namely, electrical products (copper wire, electrical plugs, pipes) and other light-industrial goods.
    - The government failed to provide adequate entrepreneurial training to local suppliers who were used to a socialist mindset.
    - In contrasts to the policies of the Kaunda government that gave preference to local suppliers, the MMD government typically, adopted a low-key approach to leverage local businesses in the mining sector. These policies of the MMD government obstruct the development of local industries and facilitated the substitution of Zambian suppliers. More specifically:
        - Besides recent ad hoc appeals to mining companies to support local suppliers, the government failed to establish definitive policies, articulating specific levels of local procurement content and skills transfer in agreements to compel TNCs to support local suppliers (as the companies function in a liberalised economy).
        - The loose commitments from companies to support procurement from local suppliers, as opposed to a legal commitment,[754] render these commitments unenforceable.
- Local suppliers having insufficient capital or access to affordable credit mainly due to:
    - The high real interest rates[755] or lending rates that increased their costs of borrowing, which is a major obstacle to the growth of the local manufacturing sector in Zambia. The high interest rate exists despite measures to improve the availability of funds in the local banks (through the lowering of the statutory reserve requirements of banks, on both the kwacha and the foreign-currency deposits), to encourage banks to cut their lending rates to the private sector.[756] The high interest rates were mainly as a consequence of:
        - The deregulation of the financial markets in the 1990s.
        - The excessive government borrowing of treasury bills in the financial market that also added to the high inflation.
        - Risk-averse tendencies of local commercial banks, rendering them unresponsive to lower private sector lending rates[757] that the BoZ encourages. These are reflected in:
            - The preference of banks to invest most of the freed-up funds instead in higher yielding government debt or treasury bills. Whilst this reduced the debt-servicing costs of the government it considerably restricts the development of the private sector.
            - The large spread between high lending rates and real negative deposit rates, owing to the low financial intermediation, despite the significant improvement of the financial sector in recent years, aided by the implementation of the government's Financial

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752 For instance, three-year tax holidays, concessions on imported mining equipment and exemptions on excise duties (including power tariffs) generally enjoyed by new foreign companies.

753 As most of Zambian copper ores are concentrated and smelted in Zambia and a number of new smelters are being built.

754 For instance, the clause in the development agreement of Bwana Mkubwa that merely indicates that mining TNCs would not discriminate against registered Zambian business, over international suppliers, proved insufficient in fostering the development of local manufacturing industries (Bwana Mkubwa Development Agreement, 2004:13).

755 The consistently high lending rates of banks in Zambia prompt companies that are able to do so, to obtain credit, especially for long-term financing requirements, from outside Zambia, which tends to be less expensive and more predictable (The Economist Intelligence Unit, 2007b:39).

756 That promoted a slight reduction in lending rates.

757 The fact that commercial banks continue to buy bonds, even when yields fall, highlights their risk-averse nature.

758 Rendering it difficult to obtain credit information on possible borrowers.

759 Which can take up to four years.

760 For about six to seven months.

761 In 2006, it cost around US$l00/ton to transport cargo from Zambia to the coast.

762 Which are not subsidised.

Sector Development Plan (FSDP).
        - The small ratio of broad money to GDP and the low private-sector credit (even compared to other sub-Saharan African countries), at less than 10% of GDP.
        - The high lending rates of banks in Zambia, despite greater macroeconomic stability in the country.
    - Higher operating costs of banks, rather than as a result of a lack of competition, as the market share of the three largest banks, at around 75%, corresponds to the average African standard. The higher operating costs of banks were mainly as a result of:
        - The high costs of transport and communications.
        - The weak credit culture,[758] with most Zambian businesses and individuals tending to default on their loans.
        - The lengthy court proceedings involved in recouping bad loans.[759]
    - A failure of the banks to generally disclose to local entrepreneurs the availability of EU and World Bank funds, placed under their care, which are at a lower interest rate than bank rates, and the stringent lending conditions attached to these loans, requiring substantial collateral.

      Accordingly, even if the spread between lending and deposit rates were to be substantially reduced, many other bank charges will keep the cost of borrowing high.
  - Accumulated arrears and delays in the ZCCM paying its debt to suppliers,[760] from 1999 to 2000, aggravated the liquidity and cash flow problems of especially those suppliers of the ZCCM that were not part of multinational corporations.
    - The payments, in many instances, were too late to save local suppliers from bankruptcy.
    - The debt to suppliers accounted for a large portion of Zambia's domestic debt prior to and immediately after the privatisation of the ZCCM. The government had to pay US$97 million to the suppliers of the ZCCM in 1999/2000 and the 2000/01 budget allocated K423 000 million for the same purpose. An EU grant to pay part of the debt to the suppliers, together with funds from the government led to all the suppliers being paid out only by 2003.
    - The establishment of the Mine Suppliers and Contractors Association only in 2000, to ensure that suppliers would be paid for services rendered to the ZCCM, were too late for many of the suppliers of the ZCCM that had already became bankrupt.
- The high costs of locally-based manufacturing companies in Zambia over foreign companies that are mainly attributable to:
  - Increases in the interest rates (especially as a result of the auctioning of the financial markets).
  - The high inflation rate (arising from cost-push inflation, following the depreciation of the kwacha that accompanied the liberalisation of the exchange rate), which increased the costs of inputs of the highly import-dependent Zambian-based manufacturing suppliers to the mines.
  - The higher utility costs, such as the steep transportation costs, the increased petroleum fuel costs and the rising electricity tariffs
    - The high production and transportation costs of Zambia,[761] owing to its landlocked status and the poor transportation system, adversely affect the competitiveness of local companies also in the export of their goods.
    - The exorbitant retail petroleum prices[762] (among the steepest in the region) which raised the transport costs in Zambia. The high retail petroleum prices were due to a weak domestic currency, high transport costs, the inability of the Indeni refinery to guarantee supplies to the energy sector and, until recently, because of the maladministration within the ZNOC. ZNOC had a monopoly in the procurement and processing of crude oil for many years. However, the liquidation of ZNOC and the government's assumption of US$150 million of the company's debt owed to the ZANACO in April 2002, may reduce the price of petroleum in the longer term.
    - The more recent increases in electricity shortages also constrained growth in the manufacturing sector.
  - The higher tax on local businesses, including excessive duties on many manufacturing inputs over foreign business.
  - Outdated technology, poorly maintained assets, high costs, under-capacity production, rising debts and poor management by some supplier companies that increases the inefficiencies of Zambian manufacturing companies.

- A weak domestic market, as a result of poor demand and purchasing power and the subdued regional market (despite increased regional integration), affecting also foreign manufacturing companies based in Zambia adversely.
- Local companies lacking aggressive marketing campaigns.

Sources: Africa Research Bulletin (2001a:14627); Aked, cited in Profit Magazine (1995a:31, 32, 34); Evans (1998); Fraser and Lungu (2007:4, 17, 58, 59, 60); Leistner (1996:11.13, 11.14, 11.20); Maambo (1998:Fig. 14); Ministry of Finance and National Planning (2002a:15); Regional Investor Survey (2001:41); SADC (2000:335); Singogo (2000:11, 12); The Economist Intelligence Unit (2002:26; 2007b:15, 25, 37, 38, 39, 42, 46, 48; 2008a:5, 6; 2008b:15, 17, 18, 20); Van Buren (2003:1153, 1154, 1155); World Bank (2002a:8; 2002b:29, 30; 2003b:132, 133); ZPA (2000a:16, 2000b:16, 2002:3) and interviews with Kojo Asiedu, 28 October 2003; Simon Capper, 30 October 2003; James Chalwe, 23 November 2003; David Chilipamushi, 20 October 2003; Valentine Chitalu, 22 October 2003; Andrew Hickman, 7 November 2003; Jack Jones, 22 October 2003; Francis Kaunda, 20 October 2003; Danny Kalyalya, 31 October 2003; Eddy Kapungulya, 13 November 2003; John Kangwa, 21 November 2003; Wilphred Katoto, 12 November 2003; Alick Lungu, 20 December 2001; John Lungu, 12 November 2003; Andygean Luombe, 8 October 2003; Charles Muchimba, 18 November 2003; Isaac Masonda, 11 November 2003; Silane Mwenechanya, 24 October 2003; Emmanuel Mutati, 18 November 2003; Fred M'membe, 14 October 2003; Ladslous Mwansa, 7 October 2003; Mark O' Donnell, 16 October 2003; Honourable Dipak Patel, 15 October 2003; M. Shandavu, 10 October 2003; Zion Simwanza, 1 December 2003; Kasote Singogo, 16 October 2003; Willie Sweta, 30 October 2003; Gilbert Temba, 18 October 2003; Fred Yamba, 25 November 2003.

Table A8: Main exploration and prospecting activities of various TNCs in Zambia

Company	Exploration and prospecting activities
Equinox Resources and Phelps Dodge	Equinox Resources and Phelps Dodge invested US$13.3 million[763] for the feasibility study of the Lumwana copper project (that is estimated to contain over 1 billion tons of low-grade copper), at the end of 2001. In 2002, Equinox Resources was to invest a further US$450 million to develop its Lumwana copper project.
Cyprus Amax	Cyprus Amax invested US$7 million, by 1998, on detailed exploration activities for copper ore bodies at Kansanshi in the North Western Province.
First Quantum	First Quantum, who subsequently bought the Kansanshi mines,[764] plans to develop reserves at Kansanshi at a capital cost of US$290 million that would considerably augment Zambia's copper production capacity.[765] In 2003, First Quantum undertook a wide-ranging grassroots exploration programme, in a joint venture with BHP Billiton who provided high technical equipment, such as the Falcon Aircraft, with drilling programmes ongoing on several targets, to search for new major copper deposits on wholly owned properties in Zambia and in the DRC.
Anglo American and Equinox Resources	Anglo American, in a joint venture partnership with Equinox Resources, participated in the US$12.5 million 'Zambezi exploration programme', established by Equinox Resources in 1999.
Mopani and Gecamine	The joint operation between Mopani and Gecamine would enable them to mine copper and cobalt deposits located on both sides of the Zambia-Congo-K frontier at Luansobe and Mufulira.[766]
AVMIN	AVMIN spent US$20 million, by 1999, on a two-year exploration and drilling programme for major copper-cobalt deposits at Konkola North, near the DRC border.

Sources: Africa Mining Intelligence (2001a:3; 2002a:3; 2002d:2, 4; 2003d:3); Ministry of Finance and Economic Development (2000:62); Maambo (1998:Fig. 13); Engineering and Mining Journal (1998:14, 1999:22); Martin Creamer's Mining Weekly (2003a, 2003c, 2003d:18).

763 Partly financed by the European Investment Bank.
764 First Quantum bought the Kansanshi mines from Phelps Dodge that in turn bought the mines from Cyprus Amax.
765 Since large deposits of copper were discovered at Kansanshi. Though the copper deposits are not of a high-grade quality they are sufficient to enable a feasible mining operation (interview with Andrew Hickman, 7 November 2003).
766 Facilitated by First Quantum's position as owner of the Dikulushi mine in Katanga.

Table A9: Technological and capital inputs from mining TNCs in the mining sector

Company	Technological and capital inputs
First Quantum	First Quantum developed the solvent extraction-electrowinning (SX/EW) facility[767] at Bwana Mkubwa,[768] to treat most oxide ores, enabling Bwana Mkubwa to expand its design output and to increase its lifespan by at least seven years. The expansion of Bwana Mkubwa's copper production capacity, under the ownership of First Quantum, enabled the company to participate in further mining acquisition and exploration activities for additional sources of oxide feed.[769] First Quantum Minerals plans to build a US$8-million sulphur burning acid plant, at its Kansanshi mining subsidiary,[770] which would enable it to produce 100 000 tons of sulphuric acid, annually, to supply the mine with all its acid requirements.[771]
MCM	New mining technology into the Nkana and Mopani mines extended mining beyond a depth of 1 340 metres[772] that boosted the life-spans of the Nkana part of the Mopani mine (from 5 years to 15-20 years) and of Mufulira (from 10 years to 25 years), from 2003.[773] The new electrolysis facility that MCM introduced, at a cost of US$5.5 million, was to maximise processing operations and boost annual production,[774] from 2001 to 2003, at the Mufulira plant at Mopani. The expansion of the productivity of the Mufulira refinery and smelter (owned by Mopani) that was working at only 65% of its capacity,[775] by 2003, will further promote the resources of the mining sector. The expansion plans were partly to accommodate plans of First Quantum to process both copper ores, imported from its mining facility at the DRC[776] and copper concentrates from Kansanshi, at the Mufulira smelter and the refinery. The expansion of the capacity of the smelter at MCM, which is able to handle 850 000 tons of ore per year, would also likely boost copper output in Zambia.
Vedanta	The KDMP[777] that Vedanta commenced in 2005, almost immediately after its takeover, in which it already committed US$750 million and invested US$400 million, from 2006-2007. The KDMP, involving a deepening of the existing mine, is expected to lift the firm's total copper output to 500 000 tons within three to four years, from a projected

767 Which provided it with the ability to treat or process conventional oxide ores from reserves at its Lonshi mining operation.
768 The company First Quantum established in 1998 as a facility to treat copper tailings.
769 The exploration activities of Bwana Mkubwa was partly achieved through significant investments in the DRC, whereby copper ore at Lonshi, about 40 km from Ndola, is trucked to Bwana Mkubwa for further processing (World Bank, 2003b:132). First Quantum obtained financing of US$6 million from Africa Merchant Bank and Banque Belgolaise SA to buy up equipment for the Lonshi copper mine, in the DRC (Africa Mining Intelligence, 2003d:3).
770 This development falls within the US$225 million of the mines' total project funds.
771 Any surplus will be exported.
772 This was accomplished partly through a loan of US$248 540 from the U.S. Trade Development Agency to the MCM, which made the feasibility study to extend Mufulira's life span possible (Africa Mining Intelligence, 2001b:3).
773 Minister Kaunda Lembalemba, cited in Martin Creamer's Mining Weekly Online, 2003c.
774 By roughly 20 000 tons.
775 Concentrates from Kansanshi might also be refined at the Nkana Smelter owned by KCM or would be exported if both the Mufulira and the Nkana smelters were to be full (Martin Creamer's Mining Weekly Online, 2003c).
776 From its Lonshi project in Congo-K that will be transported to Zambia for processing (Africa Analysis, 2001:12; Africa Mining Intelligence, 2002b:1).
777 Vedanta contracted China Nonferrous Metal Mining Company, who owns Chambishi Copper Mine, to assist in the initial work of the KDMP, namely the removal of water, the building of sinking shafts and to widen the ventilators (Africa Confidential, 2007:10).
778 Outokumpu Technology of Finland.
779 The existing smelter run by KCM for the Konkola in Nchanga, Napundwe and Nkana mines, has an annual turnover of US$75 million and employs about 14 000 people Africa Confidential, 2006:4.
780 Resident Director, cited in Fraser and Lungu, 2007:20.

Company	Technological and capital inputs
	200 000 tons in 2007. A new Finnish designed and constructed smelter[778] that Vedanta is establishing at KCM, in Chingola, at a cost of US$300 million, which was to start operations in 2008, would process about 400 000 tons of copper, annually.[779] Vedanta intends to establish a concentrator aligned to the KDMP.[780]
AVMIN	The establishment of a new plant at Chambishi, at a cost of more than US$266 million for the treatment of 20M of the Nkana smelter slag dump of AVMIN, before its departure from Zambia in 2003, constitutes a major technological investment that made possible the recovery of cobalt and copper. It was projected that the Nkana smelter slag dump would have produced about 4 000 tons of cobalt a year.[781] The smelter that AVMIN built that entered into full operation only in December 2002 (due to major operational difficulties) would have significantly augmented the cobalt and copper production levels of the company in 2003, had AVMIN not departed from Zambia.
NFCA	NFCA[782] established an ultra-modern new copper smelter, for US$220 million, at Chambishi that would produce about 150 000 tons of copper annually. The smelter of NFCA, at Chambishi, would also process ore from some mines in neighbouring Congo-Kinshasa and from the Lumwana Copper Mine, agreed to in a five-year deal.
Chibuluma	The construction of a decline shaft at Chibuluma South, in partnership with South Africa's IDC, started in September 2003, contributed to the increase in Zambia's capital stock.
CEC	CEC upgraded the power system of the Copperbelt and expanded the transmission system, with a US$10 million loan it received from the Development Bank of South Africa, in August 2000, which increased the mining sector's energy supply capacity.

Sources: Africa Analysis (2003a:16); Africa Confidential (2006:4, 2007:10); Africa Mining Intelligence (2001a:3, 2002b:1, 2007:2, 2006b:2); Engineering and Mining Journal (1999:22, 2000c:26); Fraser and Lungu (2007:20); Martin Creamer's Mining Weekly (2003b, 2003c, 2003d:18); Ministry of Finance and National Planning (2002c:61); The Economist Intelligence Unit (2007b:35, 36), World Bank (2003b:132) and interviews with Fortune Kamusaki, 25 November 2003 and John Lungu, 12 November 2003.

781 AVMIN received the bulk of its revenue from toll treatment of cobalt concentrates for KCM, MCM and RAMCOZ, before the latter went into receivership (World Bank, 2003b:132).
782 In collaboration with Yunnan Copper Industry Group.

Table A10: Institutional and regulatory measures controlling the activities of private companies in Zambia since Chiluba's government

The institutional and regulatory measures to monitor the activities of private companies, including the mining TNCs, are as follows:

- The government regulatory measures include:
  - The Companies Act, amended in 1994, which has to be in line with private ownership that confers constraints or obligations and rights to companies.
  - The Investment Act and the Mines and Minerals Act, which cover competition (monitored through the Zambian Competition Commission that was established in 1996), contracts, bankruptcy (addressed through the BoZ) and corporate governance (covered by the Companies Act). The Investment Act of 1991 was revised in 1993 and was replaced by the Investment Act of 2006.
  - A Securities and Exchange Commission, established in 1993, after the Zambian economy was liberalised to regulate the Stock Exchange and was revised in 2000, in collaboration with the Stock Exchange.
  - A new insurance law adopted in 1995, to address issues that the newly opened insurance industry faces.
  - Measures to curb money laundering:
    - The Prevention and Prohibition of Money Laundering Act was established in 2001 and the Anti-Corruption Commission (a new institution comprising of the security wing of government) that works closely with the BoZ and draws on different institutions, including the commercial banks, was instituted to address money laundering, also in the mining sector. The greater independence granted to the Anti-Corruption Commission in more recent years improved its effectiveness.
    - A change in the Banking and Financial Services Law in 1993 places all financial institutions under the supervision of the BoZ.
    - Clients are required to state the source and destination of their money and specify the purpose of money transactions of over US$5 000 and which have to be done by application.
    - The Task Force, established under the Mwanawasa government, investigates the plundering of Zambia's natural resources.

  However, the absence of exchange controls and the fact that investors are free to repatriate capital investments, dividends, management fees, profits, technical fees and royalties facilitate the outflow of mining surpluses.
- Bilateral agreements regulating the operations of mining companies in Zambia entail:
  - The sales and purchase agreement that sets out the conditions for the purchase of assets.
  - Marketing agreements established with private companies.
  - The development agreements that are bilateral agreements, comprising of commitments between the government and some mining TNCs (dealt with in Section 9 of the Mines and Minerals Act) that broadly determine the legal rules in which they would want to conduct their business. The year-by-year account of the investment and spending plans, as well as of the obligations of the mining companies, including a stipulation of the production levels that the government expects from the mining companies in the development agreements enable the government and the companies to check compliance with obligations set out in the agreements.
  - The shareholder's agreement that governs the relationship between the shareholders, including the government and the investors.
- The government bodies mandated to monitor private sector activities include:
  - The Ministry of Mines and Mineral Development and the ZCCM-IH, mandated to oversee the implementation of development agreements.
    - Directors of ZCCM-IH, on the boards of privatised mining companies, monitor whether obligations are met, in terms of investment, increasing production and in the training of manpower, as stipulated in the development agreement. The ZCCM board, under government ownership, also monitored mining-related transactions.
  - The golden share that the government enjoys, by way of the one Director representing government on the boards of each of the privatised mining companies that enables the

government to veto only those decisions deemed against the interests of the country.

- The mechanisms established through which private sector activities are monitored include:
  - Quarterly and annual returns that the mining companies submit to the Ministry of Mines and Mineral Development and to the BoZ, stipulating amongst other things the production levels and costs incurred by mining companies.
  - The customs office, which monitors the sales of cobalt.
  - The checking of company accounts, through the recently established ZRA. Transfer pricing practices of companies are, however, likely to hide the true profits of companies. International companies originating from countries that are members of the OECD having to adhere to a strict code of conduct, on account of nationals from their countries being able to seek court action against these companies.
- The monitoring of environmental pollution:
  The monitoring of environmental pollution seems less problematic on account of likely global repercussions that environmental scandals will have on the reputation of private mining companies. However, KCM and MCM, partly because of the poor environmental standards they have inherited, are exempted against adhering to certain environmental standards. The major bodies and measures established to control and monitor environmental pollution of the mining companies are:
  - The Ministry of Mines and Mineral Development, the ECZ and the Mine Safety Department.
  - Mining companies being required to submit environmental management plans that encompass environmental impact assessment reports that are open to the public, through a public disclosure process and, at times, involve various stakeholders, including villagers and the chiefs, before approval is granted.
  - Additional control that is exerted over quoted or listed companies,[783] by way of strict standards required from both the Stock Exchange, bankers that are funding the mining companies and from environmental lobby groups. A failure to meet these standards would adversely influence the share prices of listed companies.

Sources: Ministry of Mines and Mineral Development (2003:4); The Post (2003b:4); World Bank (2002b:28) and interviews with David Chilipamushi, 20 October 2003; Andrew Hickman, 7 November 2003; Reibner Hoffner, 15 October 2003; Jack Jones, 22 October 2003; Chuma Kabaghe, 18 November 2003; Thomas Kabandama, 13 November 2003; Danny Kalyalya, 31 0ctober 2003; Fortune Kamusaki, 25 November 2003; John Kangwa, 21 November 2003; Chama Kapambwe, 11 November 2003; Wilphred Katoto, 12 November 2003; Francis Kaunda, 20 October 2003; John Lungu, 12 November 2003; Charles Muchimba, 18 November 2003; Emmanuel Mutati, 18 November 2003; Fred M'muembe, 14 October 2003; Ladslous Mwansa, 7 October 2003; Bernadette Mwakacheya, 17 October 2003; Silane Mwenechanya, 24 October 2003; Dave Phiri, 23 October 2003; M. Shandavu, 10 October 2003; Willie Sweta, 30 October 2003; Dennis Wood, 21 October 2003 and Yu Zhongqin, 4 November 2003.

783 Such as Bwana Mkubwa.

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List of interviews conducted in Zambia 2003 (in chronological order)

Date	Interviewees
Tuesday, 7 October 2003	**Dr Ladslous Mwansa** Chief Economist IMF Lusaka
Wednesday, 8 October 2003	**Ms Andygean Luombe** Senior Policy Analyst National Economic Advisory Council Lusaka
Thursday, 9 October 2003	**Mr Gijs Koop** National Economist United Nations Development Programme Lusaka
Friday, 10 October 2003	**Mr M Shandavu** Ex-Company Secretary Zambia Consolidated Copper Mines (ZCCM) Lusaka
Saturday, 11 October 2003	**Dr Kenneth Kaunda** Ex-President of Zambia Lusaka
Monday, 13 October 2003	**Mr Gilbert Temba** Chairman Global Automation Zambia Ltd (GAZL) Lusaka
Tuesday, 14 October 2003	**Mr Fred M'muembe** The Zambian Post Managing Editor Lusaka **Mr Alick B. Lungu** Economist at Economic Justice Programme Catholic Centre for Justice Development and Peace Lusaka
Wednesday, 15 October 2003	**Honourable Dipak Patel** Minister Ministry of Commerce, Trade and Industry Lusaka **Mr Reibner Hoffner** Programme Manager European Development Fund Project for the Non-Traditional Mining Sector Lusaka
Thursday, 16 October 2003	**Mr Kasote Singogo** Director (Marketing and Investment Promotion) Zambia Investment Centre Lusaka **Mr Mark O' Donnell** Vice Chairman Zambia Association of Manufacturers Lusaka

Date	Interviewees
Friday, 17 October 2003	**Ms Bernadette Mwakacheya** Economist Ministry of Mines and Mineral Development Lusaka
Saturday, 18 October 2003	**Mr Gilbert Temba** Chairman Global Automation Zambia Ltd (GAZL) Lusaka
Sunday, 19 October 2003	**Mr Andrew Sardanis** Ex-Administrator of various government institutions under the Kaunda government and author of *'Africa: another side of the coin'* Lusaka
Monday, 20 October 2003	**Mr David Chilipamushi** Lecturer in Economics Copperbelt University, Kitwe Lusaka **Mr Francis Kaunda** Ex-Chairman and Chief Executive of Zambia Consolidated Copper Mines and ex-Head of GRZ/ZCCM Privatisation Negotiating Team Lusaka
Tuesday, 21 October 2003	**Mr Denis Wood** D. Wood Consultants and Investments Ltd Agri Business Consultants and Trade Finance Specialists Lusaka
Wednesday, 22 October 2003	**Mr Valentine Chitalu** Director of CDC, ex-Head of ZPA, and ex-Board member of KCM. Lusaka **Mr Jack Jones** Lecturer in Economics University of Zambia Lusaka
Thursday, 23 October 2003	**Mr David Phiri** Director of Human Resources of Anglo American and Ex-Managing Director of Roan Consolidated Mines (RCM) Lusaka **Ms Stella Mutale** Senior Economist Ministry of Finance and Economic Development Lusaka
Friday, 24 October 2003	**Dr Silane Mwenechaya** Co-ordinator The Zambian Business Forum Lusaka

Date	Interviewees
Tuesday, 28 October 2003	**Dr Kojo Asiedu** Senior Advisor Zambia-Malawi-Mozambique Triangle (ZMM-GT) United Nations Development Programme (UNDP) Lusaka **Mr Stuart Cruickshank** Advisor ZPA Lusaka
Wednesday, 29th October 2003	**Mr Gary Loop** Chief Executive Copperbelt Energy Corporation plc Lusaka **Mr L.M. Lishomwa** Ex-Economic Advisor to Ex-President Kaunda and Chairman and CEO of Guardian Motors Limited Lusaka
Thursday, 30 October 2003	**Mr Sipho Phiri and Simon Capper** Managing Directors (DCDM Accountants) and ex-Consultants (ZPA) Lusaka **Mr Willie Sweta** Ex-Director Ministry of Mines and Mineral Development Lusaka
Friday, 31 October 2003	**Dr Danny Kalyalya** Deputy Governor – Operations Bank of Zambia Lusaka
Tuesday, 4 November 2003	**Mr Yu Zhongqin** Manager of Supply and Commercial NFC Africa Mining plc Chambishi **Mr LiangTun** Manager of Finance and Budget NFC Africa Mining plc Chambishi **Mr Mwasgo Malaika** Chief Accountant NFC Africa Mining plc Chambishi
Friday, 7 November 2003	**Mr Andrew Hickman** Commercial Manager and Company Secretary Bwana Mkuba Mining Ltd (subsidiary of First Quantum Ltd) Ndola
8 November 2003	**Mr Charles Muchimba** Director Mineworkers' Union of Zambia (MUZ) Kitwe

Date	Interviewees
Sunday 9 November 2003	**Mr Eureck Chila** Coordinator of Bakabomba Trust Chambishi Metals plc Chambishi **Ms Agnes Bwalya** Chairperson of the Chambishi Bakabomba Trust Chambishi Metals plc Chambishi
Tuesday, 11 November 2003	**Mr Chama Kapambwe** Manager Refinery Chambishi Metals plc Chambishi **Mr Isaac Masonda** President Mine Suppliers & Contractors Ndola
Wednesday, 12 November 2003	**Professor John Lungu** School of Business Copperbelt University Kitwe **Mr Wilphred K. Katoto** Technical Investments Officer ZCCM Investments Holdings plc Kitwe
Thursday, 13 November 2003	**Mr Thomas Kabandama** Chief Accountant and Internal Auditor Chibuluma Mines plc Kalulushi **Mr Eddy M. Kapungulya** Honorary Secretary Kitwe District Chambers of Commerce and Industry Kitwe
Friday, 14 November 2003	**Mr Charles Muchimba** Director of Research and Organisation Mineworkers' Union of Zambia (MUZ) Kitwe
Tuesday, 18 November 2003	**Mr Charles Muchimba** Director of Research and Organisation Mineworkers' Union of Zambia (MUZ) Kitwe **Mr Emmanuel Mutati** Chief Services Officer Mopani Copper Mines plc Kitwe **Ms Chuma Kabaghe** Manager (Special Projects) Mopani Copper Mines plc Kitwe

Date	Interviewees
Friday, 21 November 2003	**Mr John Kangwa** Lecturer Land Surveyor Division Copperbelt University Kitwe
Sunday, 23 November 2003	**Mr James Chalwe** Supplier to the Mines Kitwe
Monday, 24 November 2003	**Mr Eugene B. Appel** Member of Parliament Deputy Minister (Industry) Ministry of Commerce Trade and Industry Lusaka
Tuesday, 25 November 2003	**Mr Hudson Mulumbi** Economist Ministry of Finance and National Planning Lusaka **Mr Fred Yamba** Senior Economist Ministry of Commerce Trade and Industry Lusaka **Dr Fortune Kamusaki** Senior Economist Ministry of Finance and National Planning Lusaka
Saturday, 29 November 2003	**Dr Victor C. Wells** Administrative Director/ Executive Producer Fathom Ideas Ltd Lusaka **Mr Ohene Owusu Nyanin** Country Manager (Resident Representative) The World Bank Lusaka
Monday, 1 December 2003	**Mr Zion E. Simwanza** Senior Mining Engineer (Mines Development) Ministry of Mines and Minerals Development Lusaka
Tuesday, 2 December 2003	**Mr Nchima Nchito** Lawyer Task Force (to investigate corruption during Chiluba's rule) Lusaka **Honourable Captain Moono** Member of Parliament Chilanga Constituency Lusaka
Monday, 10 January 2005	**Mr Kevin Hodges** Senior Project Manager IDC Johannesburg

List of interviews conducted in Zambia 2001 (in chronological order)

Thursday, 13 December 2001	**Mr Chansa Chifumbe Winston** Principal Mining Engineer (Projects) Ministry of Mines and Mineral Development Lusaka
Friday, 14 December 2001	**Mr Danny Kalyalya** Bank of Zambia Director of the Economics Department Lusaka
Saturday, 15 December 2001	**Mr Danny Kalyalya** Bank of Zambia Director of the Economics Department Lusaka **Mr Willie Sweta** Ministry of Mines and Mineral Development Director of the Ministry of Mines and Mineral Development Lusaka
Monday, 17 December 2001	**Mr David Chilipamushi** Copperbelt University Lecturer Kitwe **Mr Mavuto Gondwe** Mine workers' Union of Zambia (MUZ) Director of Safety and Occupational Health Kitwe **Mr Charles Muchimba** Mineworkers' Union of Zambia (MUZ) Director of Information and Research Kitwe
Tuesday, 18 December 2001	**Mr Tom Goodman** ZCCM Smelterco Limited Vice President Kitwe **Mr Lori Hanchar** ZCCM Smelterco Limited Manager Kitwe **Mr Robin Mills** Konkola Copper Mines plc Chief Operating Officer Chingola **Mr Norman B. Mbazima** Konkola Copper Mines plc Chief Financial Officer Chingola
Thursday, 20 December 2001	**Mr Alick B. Lungu** Catholic Centre for Justice Development and Peace Economist at Economic Justice Programme Lusaka